PAPER – 1: ACCOUNTING

PART – I: ANNOUNCEMENTS STATING APPLICABILITY & NON-APPLICABILITY FOR MAY, 2016 EXAMINATION

A. <u>Applicable for May, 2016 examination</u>

<u>Companies Act, 2013</u>

Relevant Sections of the Companies Act, 2013 notified up to 31st October, 2015 will be applicable for May, 2016 Examination.

B. <u>Not applicable for May, 2016 examination</u>

Ind ASs issued by the Ministry of Corporate Affairs are not applicable for the students appearing in May, 2016 Examination.

PART – II: QUESTIONS AND ANSWERS

QUESTIONS

Financial Statements of Companies

1. Ring Ltd. was registered with a nominal capital of ₹ 10,00,000 divided into shares of ₹ 100 each. The following Trial Balance is extracted from the books on 31st March, 2015:

Particulars	₹	*Particulars*	₹
Buildings	5,80,000	Sales	10,40,000
Machinery	2,00,000	Outstanding Expenses	4,000
Closing Stock	1,80,000	Provision for Doubtful Debts	6,000
Loose Tools	46,000	(1-4-2014)	
Purchases (Adjusted)	4,20,000	Equity Share Capital	4,00,000
Salaries	1,20,000	General Reserve	80,000
Directors' Fees	20,000	Profit and Loss A/c	50,000
Rent	52,000	(1-4-2014)	
Depreciation	40,000	Creditors	1,84,000
Bad Debts	12,000	Provision for depreciation:	
Investment	2,40,000	On Building 1,00,000	
Interest accrued on investment	4,000	On Machinery 1,10,000	2,10,000
Debenture Interest	56,000	14% Debentures	4,00,000
Advance Tax	1,20,000	Interest on Debentures	28,000
Sundry expenses	36,000	accrued but not due	

Debtors	2,50,000	Interest on Investments	24,000
Bank	60,000	Unclaimed dividend	10,000
	24,36,000		24,36,000

You are required to prepare statement of Profit and Loss for the year ending 31st March, 2015 and Balance sheet as at that date after taking into consideration the following information:

(a) Closing stock is more than opening stock by ₹ 1,60,000;

(b) Provide to doubtful debts @ 4% on Debtors

(c) Make a provision for income tax @30%.

(d) Depreciation expense included depreciation of ₹ 16,000 on Building and that of ₹ 24,000 on Machinery.

(e) The directors recommend a dividend @ 25% and transfer to General Reserve @ 10%.

(f) Bills Discounted but not yet matured ₹ 20,000.

2. The summarized Balance Sheet of Priya Ltd. is given below:

					(₹ in '000)
Liabilities	*31.3.14*	*31.3.15*	*Assets*	*31.3.14*	*31.3.15*
Share capital	500	500	Land & building	300	300
9% Debentures	200	160	Machinery (at cost)	164	180
Trade payables	230	216	Inventory	200	228
Profit and Loss A/c	40	54	Trade receivables	432	352
Depreciation fund	80	88	Cash and bank balances	120	110
Contingency reserve	140	110	Pre-paid expenses	4	6
Outstanding expenses	30	48			
	1,220	1,176		1,220	1,176

The following information is furnished:

(i) One old machinery which has original cost of ₹ 30,000 was sold for ₹ 10,000 in 2014-15. The accumulated depreciation in respect of the said machinery amounts to ₹ 16,000.

(ii) One new machinery was acquired for ₹ 46,000.

(iii) 9% Debentures were redeemed on 1.4.14 at a discount of 4% of their face value.

(iv) Dividend at 12% was declared and paid in cash.

(v) Income-tax liability of ₹ 30,000 paid was debited to contingency reserve. Ignore dividend distribution tax.

You are required to prepare Cash Flow Statement in accordance with the Accounting Standard 3.

Profit/Loss prior to Incorporation

3. From the following information, calculate the Ratio of Sales in each case separately.

(a) (i) Date of acquisition – 1st April, 2015; date of incorporation – 1st July, 2015 and date of closing the books of accounts – 31st March, every year.

(ii) The sales for the year ending on 31st March, 2016 were ₹ 24,00,000 of which ₹ 4,80,000 goods were sold during the first six months of the accounting period.

(b) (i) The accounts were made up to 31st December, 2015. The company was incorporated on 1st May, 2015 to take over a business from the preceding 1st January.

(ii) Total sales for the year were ₹ 12,00,000. It is ascertained that the sales for November and December are one and half times the average of those for the year, whilst those for February and April are only half the average.

(c) (i) Fema Ltd. was incorporated on 1st July, 2015 to take the existing business of X from 1stApril, 2015. Date of closing the books of account – 31st March, 2016.

(ii) Monthly sales in April 2015, February 2016 and March 2016 are double the average monthly sales for remaining months of the year.

Accounting for Bonus Issue

4. Following is the extract from the Balance Sheet of M/s. Hello Ltd. as at 31st March, 2015:

	(₹)
Authorised capital:	
50,000, 10% Preference shares of ₹ 10 each	5,00,000
2,00,000 Equity shares of ₹ 10 each	20,00,000
Issued and subscribed capital:	
40,000, 10% Preference shares of ₹ 10 each fully paid	4,00,000
1,80,000, Equity shares of ₹ 10 each, of which ₹ 7.50 paid up	13,50,000
Reserves and Surplus:	
General reserve	2,40,000
Capital reserve	1,50,000
Securities premium	30,000
Profit and loss account	3,00,000

On 1st April, 2015, the company has made a final call @ ₹ 2.50 each on 1,80,000 equity shares. The call money was received by 30th April, 2015. Thereafter the company decided to capitalize its reserves by issuing bonus shares at the rate of one share for every three shares held. Capital reserve includes ₹ 60,000 being profit on revaluation of plant and machinery.

Show necessary Journal Entries in the books of the company and prepare the extract of the Balance Sheet after bonus issue. Necessary assumption, if any, should form part of your answer.

Internal Reconstruction of a Company

5. The summarised Balance Sheet of M/s. Hema Ltd. as on 31-03-2015 is given below:

Particulars	₹	₹
1. Equity & Liabilities		
Share holder's funds: 1 lakh Equity shares of ₹ 10 each fully paid up	10,00,000	
4,000, 8% Preference shares of ₹ 100 each fully paid	4,00,000	14,00,000
2. Non- current liabilities: Long term borrowings 6% Debentures (secured by freehold property)	4,00,000	
Arrear interest	24,000	4,24,000
3. Current liabilities		
Trade payables	1,01,000	
Director's loan	3,00,000	4,01,000
		22,25,000
Assets		
1. Non- current Assets		
Fixed assets: Tangible assets		
Freehold property	5,50,000	
Plant and machinery	2,00,000	
Trade investment (at cost)	2,00,000	9,50,000
2. Current assets		
Trade receivables	4,50,000	
Inventories	3,00,000	7,50,000
3. Other assets		
Profit and loss account		5,25,000
		22,25,000

The Board of Directors of the company decided upon the following scheme of reconstruction with the consent of respective shareholders:

(i) Preference shares are to be written down to ₹ 80 each and equity shares to ₹ 2 each.

(ii) Preference dividend in arrear for 3 years to be waived by 2/3rd and for balance 1/3rd, equity shares of ₹ 2 each to be allotted.

(iii) Debentureholders agreed to take one freehold property at its book value of ₹ 3,00,000 in part payment of their holding. Balance debentures to remain as liability of the company.

(iv) Arrear debenture interest to be paid in cash.

(v) Remaining freehold property to be valued at ₹ 4,00,000.

(vi) Investment sold out for ₹ 2,50,000.

(vii) 2,25,000 of Director's loan to be waived and for the balance, equity shares of ₹ 2 each to be allotted.

(viii) 20% of Trade receivables, 40% of Inventories to be written off.

(ix) Company's contractual commitments amounting to ₹ 3,00,000 have been settled by paying 10% penalty of contract value.

Show the Journal Entries for giving effect to the internal re-construction and draw the Balance Sheet of the company after effecting the scheme. Narrations may ignored.

Amalgamation of Companies

6. A Ltd. and B Ltd. were amalgamated on and from 1st April, 2015. A new company C Ltd. was formed to take over the business of the existing companies. The draft Balance Sheets of A Ltd. and B Ltd .as at 31st March, 2015 are given below:

					(₹ in lakhs)
Liabilities	*A Ltd.*	*B Ltd.*	*Assets*	*A Ltd.*	*B Ltd.*
Share capital:			Fixed Assets:		
Equity shares of ₹ 100 each	400	375	Land & Building	275	200
12% Preference shares of ₹ 100 each	150	100	Plant & Machinery	175	125
			Investments	75	25
Reserves and surplus:			Current Assets, Loans and Advances:		
Revaluation reserve	75	50	Inventory	175	125
General reserve	85	75	Debtors	125	150

Investment allowance reserve	25	25	Bills Receivables	25	25
			Cash and Bank balances	150	100
Profit and Loss Account	25	15			
Secured loan:					
10%Debentures (₹ 100 each)	30	15			
Current liabilities and provisions:					
Creditors	135	60			
Acceptance	75	35			
	1,000	750		1,000	750

Additional information:

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

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

(c) 10% Debentureholders of A Ltd. and B Ltd. are discharged by C Ltd., issuing such number of its 15% Debentures of ₹ 100 each so as to maintain the same amount of interest.

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

(e) Liquidation expenses are:

A Ltd. ₹ 2,00,000

B Ltd. ₹ 1,00,000

It was decided that these expenses would be borne by C Ltd.

(f) All the assets and liabilities of A Ltd. and B Ltd. are taken over at book value.

(g) Authorised equity share capital of C Ltd. is ₹ 5,00,00,000, divided into equity shares of ₹ 10 each. After issuing required number of shares to the Liquidators of A Ltd. and B Ltd., C Ltd. issued balance shares to Public. The issue was fully subscribed.

Required:

Prepare the Balance Sheet of C Ltd. as at 1st April, 2015 after amalgamation has been carried out on the basis of Amalgamation in the nature of purchase.

Average Due Date

7. Find out Due date of Maturity, in case of following Bills of Exchange, where maturity period of the bill is one month:

   Date of Bill:

   (i) 26th January, 2016

   (ii) 23rd December, 2014

   (iii) 13th January, 2015 (day on which Bill of Exchange is at maturity, after including days of grade, declared as holiday due to some emergency),

   (iv) 13th July, 2015 (day on which Bill of Exchange is at maturity, after including days of grace, is Sunday).

Account Current

8. Mr. Abhinav has opened an overdraft account with a Bank on 1st April, 2015. He deposited ₹ 40,000 as cash on the same day. His other deposits and withdrawals for the month of April 2015 were as below:

	₹
Deposits:	
10th April,2015	60,000
18th April,2015	68,000
Withdrawals:	
5th April,2015	1,20,000
16th April,2015	80,000
25th April,2015	1,00,000

Bank charges interest @12% p.a. on debit balance. No interest allowed on credit balance. Prepare Account current for the month of April, 2015, in the books of Bank, by means of product of balances. Bank debits interest in account twice during the month i.e. 15th and 30th/31st (as the case may be) of a particular month. For the purpose of calculation of interest, year should be treated as of 365 days. Round off all the calculations to the nearest rupee.

Self Balancing Ledgers

9. From the following prepare General Ledger Adjustment account in Debtors Ledger and Debtors Ledger Adjustment account in General Ledger:

	₹
Balance as on 1.4.2015:	
Debit balances in Debtors ledger	2,46,200

Credit balances in Debtors ledger	3,400
Transactions during the month of April, 2015:	
Credit sales	9,74,900
Sales return	21,700
Cash received from debtors	8,62,100
Discount allowed to debtors	39,200
Bills receivable received from debtors	51,200
Bills receivable dishonoured	3,500
Bills payable given to suppliers	27,000
Credit balance in Debtors ledger on 30.4.2015	5,200

Financial Statements of Not for Profit Orgnisations

10. Doctor Dinesh after retiring from Govt. service, started private practice on 1st April, 2014 with ₹ 1,00,000 of his own and ₹ 1,50,000 borrowed at an interest of 12% per annum on the security of his life policies. His accounts for the year were kept on a cash basis and the following is his summarized cash account:

Receipts	₹	*Payments*	₹
Own capital	1,00,000	Medicines purchased	1,22,500
Loan	1,50,000	Surgical equipments	1,25,000
Prescription fees	3,30,000	Motor car	1,60,000
Visiting fees	1,25,000	Motor car expenses	60,000
Fees from lectures	12,000	Wages and salaries	52,500
Pension received	1,50,000	Rent of clinic	30,000
		General charges	24,500
		Household expenses	90,000
		Household Furniture	12,500
		Expenses on daughter's marriage	1,07,500
		Interest on loan	18,000
		Balance at bank	55,000
		Cash in hand	9,500

One-third of the motor car expense may be treated as applicable to the private use of car and ₹ 15,000 of salaries are in respect of domestic servants.

The stock of medicines in hand on 31st March, 2015 was valued at ₹ 47,500.

You are required to prepare his capital account and income and expenditure account for the year ended 31st March, 2015 and balance sheet as on that date. Ignore depreciation of fixed assets.

Accounts from Incomplete Records

11. Assets and Liabilities of Ms. Shreya, who runs a Beauty Saloon, as on 31-03-2014 and 31-03-2015 are as follows:

	31-03-2014 (₹)	*31-03-2015 (₹)*
Assets:		
Machinery & Tools	25,000	30,000
Furniture & Fixtures	50,000	60,000
Stock of Consumables	60,000	1,35,000
Sundry Debtors	20,000	45,000
Cash at Bank	35,000	42,500
Cash in Hand	2,150	3,750
Liabilities:		
Loans (Principal)	50,000	40,000
Sundry Creditors	20,000	35,000

Depreciation on Machinery & Tools and Furniture & Fixture to be provided on W.D.V. method @ 10% p.a. during FY 2014-15. Shreya has purchased Machinery & Tools amounting to ₹ 5,000 on 01-07-2014. She has also purchased Furniture & Fixture amounting to ₹ 10,000 on 01-01-2015. Loan amount of Rs. 10,000 was partly paid by her on 31-03-2015. Interest on Loan to be provided @ 12 p.a. and same is unpaid as on 31-03-2015. No interest of earlier period is outstanding. During FY 2014-15, Shreya participated in a competition and won a prize of ₹ 20,000. Same is retained by her in the business. Monthly withdrawals of Shreya were ₹ 1,000 during FY 2014-15. Prepare Statement of Affairs and determine Profit for the FY ending as on 31-03-2015 by applying the method of the Capital Comparison.

Hire Purchase Transactions

12. On 1st April, 2012, X Ltd. sells a Trucks on hire purchase basis to X Transporters & Co. for a total purchase price of ₹ 18,00,000 payable as to ₹ 4,80,000 as down payment and the balance in three equal annual instalments of ₹ 4,40,000 each payable on 31st March 2013, 2014 and 2015.

The hire vendor charges interest @ 10% per annum.

You are required to ascertain the cash price of the truck for X Transporters & Co. Calculations may be made to the nearest rupee.

Investment Accounts

13. The following information is presented by Mr. Akash relating to his holding in 9% Government Bonds:

    Opening Balance as on 01-01-2014 (Face Value) ₹ 60,000, Cost ₹ 59,000 (Face value of each unit is ₹ 100)

    01-03-2014 purchased 100 units, ex-interest at ₹ 100

    01-07-2014 sold 250 units, ex-interest out of original holding at ₹ 100

    01-10-2014 Purchased 75 units at ₹ 98 cum interest.

    01-11-2014 sold 150 units ex-interest at ₹ 99 out of original holdings.

    Interest due dates are 30th September and 31st March, Mr. Akash closes his books every year by 31st December.

    Show the Investment A/c as it would appear in his books. Mr. Akash was following FIFO Method.

Insurance claim for loss of stock

14. On 13th September, 2014 fire occurred in the premises of M/s DEF & Co. Most of the stocks were destroyed. Cost of stock salvaged being ₹ 40,000. In addition some stock was salvaged in damaged condition and its value in that condition agreed at ₹ 20,000. From the salvaged accounting records, the following information is available:

	₹
Stock of goods @ 10% lower than cost as on 31st March, 2014	8,64,000
Purchases (1.4.14 to 13.09.14)	35,29,900
Sales (1.4.14 to 13.09.2014)	46,93,200

Additional information:

(1) Sales upto 13th September, 2014, includes ₹ 70,000 for which goods had not been dispatched and ₹ 25,000 of goods sent on approval basis but approval for which not received.

(2) Purchases upto 13th September, 2014 did not include ₹ 60,000 for which purchase invoices had not been received from suppliers, though goods have been received in Godown. Further purchases include purchase of machinery costing ₹ 40,000.

(3) Past records show the gross profit rate of 25%.

(4) M/s DEF & Co. has insured their stock for ₹ 9,00,000.

Find out the value of loss of stock by applying the above points.

Issues in Partnership Accounts

15. The Balance Sheet of a Partnership Firm M/s AB & Co consisted of two partners A and B who were sharing Profits and Losses in the ratio of 5 : 3 respectively. The position as on 31-03-2015 was as follows:

Liabilities	₹	*Assets*	₹
A's Capital	4,10,000	Land & Building	3,80,000
B's Capital	3,30,000	Plant & Machinery	1,70,000
Profit & Loss *A/c*	1,12,000	Furniture	1,09,480
Trade Creditors	54,800	Stock	1,45,260
		Sundry debtors	60,000
		Cash at Bank.	42,060
	9,06,800		9,06,800

On the above date, C was admitted as a partner on the following terms:

(a) C should get 1/5th of share of profits.

(b) C brought ₹ 2,40,000 as his capital and ₹ 32,000 for his share of Goodwill.

(c) Plant and Machinery would be depreciated by 15% and Land & Buildings would be appreciated by 40%.

A provision for doubtful debts to be created at 5% on sundry debtors.

An unrecorded liability of ₹ 6,000 for repairs to Buildings would be recorded in the books of accounts.

(d) Immediately after C's admission, Goodwill brought by him would be adjusted among old partners. Thereafter, the capital accounts of old partners would be adjusted through the current accounts of partners in such a manner that the capital accounts of all the partners would be in their profit sharing ratio.

Prepare Revaluation A/c, Capital Accounts of the partners, New profit sharing ratio and Balance Sheet of the Firm after the admission of C.

Accounting in Computerised Environment

16. What are the advantages of spread-sheet software as an accounting tool?

Applicability of Accounting Standards

17. (a) What are the issues with which Accounting Standards deal?

AS 1 Disclosure of Accounting Policies

(b) XYZ Company is engaged in the business of financial services and is undergoing tight liquidity position, since most of the assets of the company are blocked in various claims/petitions in a Special Court. XYZ has accepted Inter-Corporate Deposits (ICDs) and, it is making its best efforts to settle the dues. There were claims at varied rates of interest, from lenders, from the due date of ICDs to the date of repayment. The company has provided interest, as per the terms of the contract till the due date and a note for non-provision of interest on the due date to date of repayment was affected in the financial statements. On account of uncertainties existing regarding the determination of the amount and in the absence of any specific legal obligation at present as per the terms of contracts, the company considers that these claims are in the nature of "claims against the company not acknowledged as debt", and the same has been disclosed by way of a note in the accounts instead of making a provision in the profit and loss accounts. State whether the treatment done by the Company is correct or not.

AS 2 Valuation of Inventories

18. (a) On the basis of information given below, find the value of inventory (by periodic inventory method) as per AS 2, to be considered while preparing the Balance Sheet as on 31st March, 2015 on weighted Average Basis.

Details of Purchases:

Date of purchase	Unit (Nos.)	Purchase cost per unit (₹)
01-03-2015	20	108
08-03-2015·	15	107
17-03-2015	30	109
25-03-2015	15	107

Details of issue of Inventory:

Date of Issue	Unit (Nos.)
03-03-2015	10
12-03-2015	20
18-03-2015	10
24-03-2015	20

Net realizable value of inventory as on 31st March, 2015 is ₹ 107.75 per unit. What will be the value of Inventory as per AS 2?

AS 3 Cash flow Statements

(b) Classify the following activities as (i) Operating Activities, (ii) Investing Activities, (iii) Financing Activities (iv) Cash Equivalents.

a. Purchase of Machinery.

b. Proceeds from issuance of equity share capital

c. Cash Sales.
d. Proceeds from long-term borrowings.
e. Proceeds from Trade receivables.
f. Cash receipts from Trade receivables.
g. Trading Commission received.
h. Purchase of investment.
i. Redemption of Preference Shares.
j. Cash Purchases.
k. Proceeds from sale of investment
l. Purchase of fixed asset.
m. Cash paid to suppliers.
n. Interim Dividend paid on equity shares.
o. Wages and salaries paid.
p. Proceed from sale of patents.
q. Interest received on debentures held as investment.
r. Interest paid on Long-term borrowings.
s. Office and Administration Expenses paid
t. Manufacturing Overheads paid.
u. Dividend received on shares held as investments.
v. Rent received on property held as investment.
w. Selling and distribution expense paid.
x. Income tax paid
y. Dividend paid on Preference shares.
z. Underwritings Commission paid.
aa. Rent paid.
bb. Brokerage paid on purchase of investments.
cc. Bank Overdraft
dd. Cash Credit
ee. Short-term Deposits
ff. Marketable Securities
gg. Refund of Income Tax received.

AS 6 Depreciation Accounting

19. (a) A computer costing ₹ 1.2 lakh is depreciated on straight line basis, assuming 10 years working life and Nil residual value, for three years. The estimate of remaining useful life after third year was reassessed at 5 years. Calculate depreciation as per the provisions of Accounting Standard 6 "Depreciation Accounting".

AS 7 Construction Contracts

(b) Five Star Construction Limited commenced a construction contract on 1st April, 2014. The Fixed Contract price agreed was ₹ 50,00,000. The company incurred ₹ 21,00,000 in 2014-15 for 40% work and received ₹ 19,00,000 as progress payment from the customer. The company estimated that a further ₹ 31,50,000 would incurred to complete it. What amount should be charged to revenue for the year 2014-15 as per AS 7? Show the extract of Profit & Loss A/c for the year 2014-15 in the books of the company.

AS 9 Revenue Recognition

20. (a) X Limited sold goods worth ₹ 13 Lakhs to Mr. Y. Mr. Y asked for a Trade Discount amounting to ₹ 1,06,000 and the same was agreed to by X Limited. Such discount was allowed in the ordinary course of business. The sale was effected and goods were dispatched. On receipt of goods, Mr. Y has found that goods worth ₹ 1,34,000 are defective. Mr. Y returned defective goods to X Limited and made payment amount to ₹ 10,60,000. The Accountant of X Limited booked the sale for ₹ 10,60,000.

Discuss the contention of the Accountant with reference to relevant Accounting Standard.

AS 10 Accounting for Fixed Assets

(b) XYZ Ltd. constructed a fixed asset and incurred the following expenses on its construction:

	₹
Materials	10,00,000
Direct Labour	3,00,000
(1/6th of the total labour time was chargeable to the construction)	
Direct Expenses	2,00,000
Office & Administrative Expenses	7,50,000
(5% is specifically attributable to construction)	
Depreciation on assets used for the construction of this asset	10,000

Calculate the cost of the fixed asset.

SUGGESTED ANSWERS / HINTS

1. **Ring Ltd.**

Profit and Loss Statement for the year ended 31st March, 2015

	Particulars	Note No.	(₹ In lacs)
I	**Revenue from operations**		10,40,000
II	**Other income**		24,000
III	**Total Revenue [I + II]**		10,64,000
IV	**Expenses:**		
	Cost of purchase [4,20,000+ 1,60,000]		5,80,000
	Changes in inventories [20,000-1,80,000]		(1,60,000)
	Employee Benefits Expense		1,20,000
	Finance Costs		56,000
	Depreciation and Amortization Expenses		40,000
	Other Expenses	8	1,24,000
	Total Expenses		7,60,000
V	**Profit before Tax (III-IV)**		3,04,000
VI	**Tax Expenses @ 30%**		(91,200)
VII	**Profit for the period**		2,12,800

Balance Sheet of Ring Ltd. as at 31ST March, 2015

Particulars	Note No.	₹
I **EQUITY AND LIABILITIES**		
(1) **Shareholders' Funds**		
(a) Share Capital	1	4,00,000
(b) Reserves and Surplus	2	2,22,442
(2) **Non-Current Liabilities**		
(a) Long-term Borrowings (Debentures)		4,00,000
(3) **Current Liabilities**		
(a) Trade Payable (Sundry Creditors)		1,84,000
(b) Other Current Liabilities	3	42,000
(c) Short-Term Provisions	4	2,11,558
Total		14,60,000

II ASSETS		
(1) Non-Current Assets		
(a) Fixed Assets		
(i) Tangible Assets	5	5,70,000
(b) Non-current Investments		2,40,000
(2) Current Assets		
(a) Inventories	6	2,26,000
(b) Trade Receivables	7	2,40,000
(c) Cash and Cash equivalents		60,000
(d) Short Term Loans and Advances (Advance Payment of Tax)		1,20,000
(e) Other Current Assets		4,000
(Interest accrued on investments)		
Total		**14,60,000**

Note: There is a Contingent Liability for bills discounted but not yet matured amounting ₹ 20,000.

Notes to Accounts:

1.	**Share Capital**		
	Authorized Capital		
	10,000 Equity Shares of ₹ 100 each		10,00,000
	Issued Capital		
	4,000 Equity Shares of ₹ 100 each		4,00,000
	Subscribed Capital and fully paid		
	4,000 Equity Shares of ₹ 100 each		4,00,000
			4,00,000
2.	**Reserve and Surplus**		
	General Reserve [₹ 80,000 + ₹ 21,280]		1,01,280
	Balance of Statement of Profit & Loss Account		
	Opening Balance	50,000	
	Add: Profit for the period	2,12,800	
		2,62,800	
	Appropriations		
	Transfer to General Reserve @ 10%	(21,280)	

	Proposed Equity Divided [25% of ₹ 4,00,000]	(1,00,000)	
	Dividend Distribution Tax (W. N.1)	(20,358)	1,21,162
			2,22,442
3.	**Other Current Liabilities**		
	Unclaimed Dividend		10,000
	Outstanding Expenses		4,000
	Interest accrued on Debentures		28,000
			42,000
4.	**Short-Term Provision**		
	Provision for Tax		91,200
	Proposed Equity Dividend		1,00,000
	Dividend Distribution Tax		20,358
			2,11,558
5	**Tangible Assets**		
	Buildings	5,80,000	
	Less: Provision for Depreciation	1,00,000	4,80,000
	Plant and Equipment	2,00,000	
	Less: Provision for Depreciation	1,10,000	90,000
			5,70,000
6	**Inventories**		
	Closing Stock of Finished Goods	1,80,000	
	Loose Tools	46,000	2,26,000
7	**Trade Receivables**		
	Sundry Debtors	2,50,000	
	Less: Provision for Doubtful Debts	(10,000)	2,40,000
8.	**Other Expenses**		
	Rent		52,000
	Miscellaneous Expenses		36,000
	Directors' Fees		20,000
	Bad Debts		12,000
	Provision for Doubtful Debts (4% of ₹ 2,50,000 less ₹ 6,000)		4,000
			1,24,000

Working Note

Calculation of Dividend distribution tax

Particulars	₹
(i) Grossing-up of dividend	
Dividend distributed by Ring Ltd. 25% of 4,00,000	1,00,000
Add: Increase for the purpose of grossing up of dividend [1,00,000 x (15/(100-15)]	17,647
Gross dividend	1,17,647
(ii) Dividend distribution tax @ 17.304% of ₹ 1,17,647	20,358

2. Cash Flow Statement of Priya Ltd.

for the year ended 31st March, 2015

		₹	₹
A. Cash flow from Operating Activities			
Net profit before tax (₹ 54,000 – ₹ 40,000 + ₹ 60,000)		74,000	
Add: Adjustment for depreciation (W.N.1)		24,000	
Interest on debentures (₹ 1,60,000 x 9%)		14,400	
Loss on sale of machinery (W.N.2)		4,000	
		1,16,400	
Less: Profit on redemption of debentures (Non Operating Income)		(1,600)	
		1,14,800	
*Less :*Income tax paid		(30,000)	
Operating profit before changes in Working Capital		84,800	
Add: Increase in outstanding expenses	18,000		
Decrease in trade receivables	80,000	98,000	
		1,82,800	
Less: Decrease in trade payables	14,000		
Increase in inventory	28,000		
Increase in prepaid expenses	2,000	(44,000)	
Net cash from operating activities			1,38,800
B. Cash flow from Investing Activities			
Sale of old machinery		10,000	

Purchase of machinery	(46,000)	
Net cash used in investing activities		(36,000)
C. Cash flow from Financing Activities		
Redemption of debentures (₹ 40,000 – ₹ 1,600)	(38,400)	
Payment of dividend	(60,000)	
Payment of interest on debentures	(14,400)	
Net cash used financing activities		(1,12,800)
Net decrease in cash and cash equivalents during the year		(10,000)
Cash and cash equivalents at the beginning of the year		1,20,000
Cash and cash equivalents at the end of the year		1,10,000

Working Notes:

1. Depreciation Fund

	₹		₹
To Machinery A/c	16,000	By Balance b/d	80,000
To Balance c/d	88,000	By Profit and Loss A/c (Current year depreciation)	24,000
	1,04,000		1,04,000

2. Machinery A/c

	₹		₹
To Balance b/d	1,64,000	By Depreciation Fund	16,000
To Bank (Purchased)	46,000	By Bank (realized on sale of old machinery	10,000
		By Profit and loss A/c (loss on sale) – Balancing Fig	4,000
		By Balance c/d	1,80,000
	2,10,000		2,10,000

3. **(a)** Sales of first 6 months = ₹ 4,80,000. Average sale of first 6 months = ₹ 4,80,000/6 = ₹ 80,000 per month. Pre-incorporation period consist of 3 months (i.e., April, May and June). The sales of those 3 months = ₹ 80,000 x 3 = ₹ 2,40,000. Sales of remaining 9 months = ₹ 24,00,000 – ₹ 2,40,000 = ₹ 21,60,000.

Therefore, the ratio of sales = ₹ 2,40,000 : ₹ 21,60,000 or 1: 9.

(b) Let the average of monthly sales = X. The sales of different months can be shown as follows:

Month	Jan	Feb	Mar.	April	May	June	July	Aug	Sept	Oct	Nov	Dec
Sales	1x	0.5x	1x	0.5x	1x	1x	1x	1x	1x	1x	1.5x	1.5x

Date of incorporation is May, 2015

Pre incorporation period is from January to April i.e. 3 x

Post - incorporation period is from May to December i.e 9x

The ratio of Sales = 3x : 9x or 1:3.

(c) Let the average monthly sales be x. The sales of different months can be shown as follows:

Month	April	May	June	July	Aug.	Sept	Oct	Nov	Dec	Jan	Feb	March
Sales	2x	1x	1x	1x	1x	1x	1x	1x	1x	1x	2x	2x

Date of incorporation is 1 July, 2015

Pre incorporation period is from April to June i.e. 4 x

Post - incorporation period is from July to March i.e 11x

The ratio of Sales = 4x : 11x or 4:11

4. **In the books of M/s. Hello Ltd.**

Journal Entries

Date	*Particulars*		₹	₹
1.4.2015	Equity share final call A/c	Dr.	4,50,000	
	To Equity share capital A/c			4,50,000
	(Being the final call of ₹ 2.50 per share on 1,80,000 equity shares made)			
30.4.2015	Bank A/c	Dr.	4,50,000	
	To Equity share final call A/c			4,50,000
	(Being final call money on 1,80,000 shares received)			
30.4.2015	Securities premium A/c	Dr.	30,000	
	Capital reserve A/c (1,50,000 – 60,000)	Dr.	90,000	
	General reserve A/c	Dr.	2,40,000	
	Profit and loss A/c	Dr.	2,40,000	
	To Bonus to shareholders A/c			6,00,000
	(Being utilisation of reserves for bonus issue of one share for every three shares held)			
30.4.2015	Bonus to equity shareholders A/c	Dr.	6,00,000	
	To Equity share capital A/c			6,00,000
	(Being capitalization of the bonus shares issued)			

Extract of Balance Sheet (After bonus issue)

Particulars	*Notes No.*	₹
Equity & liabilities		
1. Shareholders' Funds		
(a) Share Capital	1	28,00,000
(b) Reserves & Surplus	2	1,40,000

Notes to Accounts

		₹
1. Share Capital		
Authorised share capital:		
50,000, 10% Preference shares of ₹ 10 each		5,00,000
2,40,000, Equity shares of ₹ 10 each (refer W.N.)		24,00,000
Issued and subscribed capital:		
40,000, 10% Preference shares of ₹ 10 each fully paid		4,00,000
2,40,000, Equity shares of ₹ 10 each fully paid		24,00,000
(Out of the above, 60,000 equity shares of ₹ 10 each have been issued by way of bonus)		
		28,00,000
2. Reserves and Surplus:		
General reserve	2,40,000	
Less: Utilisation for issue of bonus shares	(2,40,000)	-
Capital reserve	1,50,000	
Less: Utilisation for issue of bonus shares	(90,000)	60,000
Securities premium	30,000	
Less: Utilisation for issue of bonus shares	(30,000)	-
Profit and loss A/c	3,00,000	
Less: Utilisation for issue of bonus shares	(2,40,000)	60,000
		1,20,000

Assumptions:

1. Capital Reserve collected in cash only can be utilized for the purpose of issue of bonus shares. Hence, capital reserve representing profit on revaluation of machinery has not been used for the purpose of issue of bonus shares. It is assumed that balance of capital reserve is collected in cash only.

2. It is also assumed that necessary resolutions have been passed and requisite legal requirements related to the issue of bonus shares have been complied with before issue of bonus shares.

Working Note:

On the basis of the above assumptions, the Authorised Capital should be increased as under:

Required for bonus issue	₹ 6,00,000
Less: Balance of authorised equity share capital (available)	(₹ 2,00,000)
Authorised capital to be increased	₹ 4,00,000
Total authorised capital after bonus issue (₹ 20,00,000 + ₹ 4,00,000) =	₹ 24,00,000

5. In the books of Hema Ltd.

Journal Entries

	Particulars		*Debit* ₹	*Credit* ₹
i	8% Preference share capital A/c (₹ 100 each)	Dr.	4,00,000	
	To 8% Preference share capital A/c (₹ 80 each)			3,20,000
	To Capital reduction A/c			80,000
ii	Equity share capital A/c (₹ 10 each)	Dr.	10,00,000	
	To Equity share capital A/c (₹ 2 each)			2,00,000
	To Capital reduction A/c			8,00,000
iii	Capital reduction A/c	Dr.	32,000	
	To Equity share capital A/c (₹ 2 each)			32,000
iv	(a) 6% Debentures A/c	Dr.	3,00,000	
	To Debenture holders A/c			3,00,000
	(b) Debenture holders A/c	Dr.	3,00,000	
	To Freehold property A/c			3,00,000
v	Accrued debenture interest A/c	Dr.	24,000	
	To Bank A/c			24,000
vi	Freehold property A/c	Dr.	1,50,000	
	To Capital reduction A/c			1,50,000
vii	Bank A/c	Dr.	2,50,000	
	To Trade investment A/c			2,00,000
	To Capital reduction A/c			50,000

vii	Director's loan A/c	Dr.	3,00,000	
	To Equity share capital A/c (₹ 2 each)			75,000
	To Capital reduction A/c			2,25,000
ix	Capital Reduction A/c	Dr.	7,65,000	
	To Profit and loss A/c			5,25,000
	To Trade receivables A/c			90,000
	To Inventories A/c			1,20,000
	To Bank A/c (10% of ₹ 3,00,000)			30,000
x	Capital Reduction A/c	Dr.	5,08,000	
	To Capital reserve A/c			5,08,000

Balance Sheet of Hema Ltd. (and reduced)

Particulars	*Notes No.*	₹
Equity and Liabilities		
1 Shareholders' funds		
a Share capital	1	6,27,000
b Reserves and Surplus	2	5,08,000
2 **Non-current liabilities**		
Long-term borrowings	3	1,00,000
3 **Current liabilities**		
a Trade Payables		1,01,000
Total		13,36,000
Assets		
1 **Non-current assets**		
a Fixed assets		
Tangible assets	4	6,00,000
2 **Current assets**		
a Inventories		1,80,000
b Trade receivables		3,60,000
c Cash and cash equivalents	5	1,96,000
Total		13,36,000

Note to Accounts

		₹
1.	**Share Capital**	
	1,53,500 Equity shares of ₹ 2 each	3,07,000
	(out of which 53,500 shares have been issued for consideration other than cash)	
	4,000, 8% Preference shares of ₹ 80 each fully paid up	3,20,000
	Total	6,27,000
2.	**Reserves and Surplus**	
	Capital Reserve	5,08,000
3.	**Long-term borrowings**	
	Secured	
	6% Debentures	1,00,000
4.	**Tangible assets**	
	Freehold property	4,00,000
	Plant and machinery	2,00,000
	Total	6,00,000
5.	**Cash and cash equivalents**	
	Cash at bank (2,50,000 – 24,000 –30,000)	1,96,000

6. Balance Sheet of C Ltd. as at 1st April, 2015

Particulars	*Notes No.*	*(₹ in Lakhs)*
EQUITY AND LIABILITIES		
1 Shareholders' funds		
a) Share capital	1	750
b) Reserves and Surplus	2	875
2 Non-current liabilities		
Long-term borrowings	3	30
3 Current liabilities		
Trade Payables	4	305
Total		1,960
ASSETS		
1 Non-current assets		
a) Fixed assets		
i) Tangible assets	5	775

	ii) Intangible assets	6	13
b)	Non-current investments	7	100
	Other non-current assets	8	50
2	**Current assets**		
a)	Inventories(175+125)		300
b)	Trade receivables	9	325
c)	Cash and cash equivalents	10	397
	Total		1,960

Notes to Accounts

		(₹ in Lakhs)
1.	**Share Capital**	
	Authorised share capital:	
	50,00,000 Equity shares of ₹ 10 each	500
	Issued and subscribed:	
	50,00,000 Equity shares of ₹ 10 each	500
	2,50,000 Preference shares of ₹ 100 each	250
	(Of the above shares 35,00,000 equity shares and all preference shares are allotted as fully paid up for consideration other than cash)	
	Total	750
2.	**Reserves and Surplus**	
	Securities premium (₹ 50 per Preference share on 2.5 Lakh Preference Shares + ₹ 20 per equity share on 35 Lakh equity shares issued to shareholders of A Ltd. & B Ltd. = ₹ 825 Lakhs)	825
	Investment allowance reserve (25+25)	50
	Total	875
3.	**Long-term borrowings**	
	Secured	
	15% Debentures	30
	Interest on Debentures of A Ltd is ₹ 3 Lakhs and of B Ltd is ₹ 1.5 Lakhs. Total int = ₹ 4.5 Lakhs. 15% debentures to be issued to equal interest of ₹ 4.5 Lakhs = ₹ 4.5 Lakhs / 15% = 30 Lakh 15% Debentures of ₹ 100 each = 30,000 debentures	

4.	**Trade Payables**		
	Acceptances (75+35)		110
	Creditors (135+60)		195
		Total	305
5.	**Tangible assets**		
	Land and building (275+200)		475
	Plant and machinery (175+125)		300
		Total	775
6.	**Intangible assets**		
	Goodwill (10+2+1)		13
7.	**Non-current investments**		
	Other non-current investments(75+25)		100
8.	**Other non-current assets**		
	Amalgamation adjustment account		50
9.	**Trade receivables**		
	Debtors (125+150)		275
	Bills receivables (25+25)		50
		Total	325
10	**Cash and cash equivalents**		
	Cash and bank (250+150-3)		397

Working Notes:

1.

Computation of Purchase Consideration			*₹ in lakhs*	
			A Ltd.	*B Ltd.*
(a)	Preference shareholders:			
	1,50,00,000/100 = 1,50,000 shares			
	Share capital = 1,50,000 shares × ₹ 100 each	150		
	Securities premium = 1,50,000 shares × ₹ 50 each	75	225	
	1,00,00,000/100 = 1,00,000 shares			
	Share capital = 1,00,000 shares × ₹ 100 each	100		
	Securities premium= 1,00,000 shares × ₹ 50 each	50		150
(b)	Equity shareholders:			
	4,00,00,000/100 × 5 = 20,00,000 shares			

	Share capital = 20,00,000 shares × ₹ 10 each 200		
	Securities premium=20,00,000 shares× ₹ 20 each 400	600	
	3,75,00,000/100 × 4 = 15,00,000 shares		
	Share capital = 15,00,000 shares ×₹ 10 each 150		
	Securities premium = 15,00,000 shares ×₹ 20 each 300		450
	Amount of purchase consideration	825	600
2.	**Calculation of number of debentures issued**	*₹ in lakhs*	
		A Ltd.	*B Ltd.*
	10% Debentures of ₹ 100 each	30	15
	15% Debentures to be issued to maintain same amount of interest:		
	Interest = ₹ 30,00,000 x 10% = ₹ 3,00,000		
	Value of 15% Debentures = $\frac{₹\,3,00,000}{15}\times 100$	20	
	Interest = ₹ 15,00,000 x 10%		
	Value of 15% Debentures = $\frac{₹\,1,50,000}{15}\times 100$		10
3.	**Net assets taken over**	*₹ in lakhs*	
		A Ltd.	*B Ltd.*
	Assets taken over		
	Land and building	275	200
	Plant and machinery	175	125
	Investments	75	25
	Inventory	175	125
	Debtors	125	150
	Bills receivable	25	25
	Cash and bank	150	100
		1,000	750
	Less: Liabilities taken over		
	Debentures	20	10
	Creditors	135	60
	Bills payable	75	35
		230	105

Net assets taken over	770	645
Purchase consideration	825	600
(Goodwill)/ Capital Reserve	(55)	45
Net goodwill		(10)

4. As the Liquidation expenses of A Ltd. and B Ltd., ₹ 2 lakhs and ₹ 1 lakhs respectively are borne by C Ltd. the same will be debited to Goodwill account in the books of C Ltd.

7. Due date of maturity:

(i) 29th February, 2016. Year 2016 being leap year, due date will be 29th February, 2016.

(ii) 25th January, 2015. Due date, after grace days, is 26th January, 2015, but since 26th January, 2015 is holiday, due date will be 25th January, 2015.

(iii) 17th February, 2015. Due date after grace days, is 16th February, 2015, but since due to some emergency, it is declared as holiday, due date will be 17th February, 2015.

(iv) 14th August, 2015. Due date after grace days, is 16th August,2015 but since 16th August,2015 is holiday(Sunday) and 15th August,2015 is also holiday, due date will be 14th August,2015.

8. In the books of Bank

Account Current of Mr. Abhinav for the month ending April 2015

Date	*Particulars*	*Dr.*	*Cr.*	*Dr. or Cr.*	*Balance*	*Days*	*Product*
2015							
1st April	By Cash	–	40,000	Cr.	40,000		–
5th April	To Cash	1,20,000	–	Dr.	80,000	5	4,00,000
10th April	By Cash	–	60,000	Dr.	20,000	5	1,00,000
15th April	To interest	164	–	Dr.	20,164	1	20,164
16th April	To Cash	80,000	–	Dr.	1,00,164	2	2,00,328
18th April	By Cash	-	68,000	Dr.	32,164	7	2,25,148
25th April	To cash	1,00,000	-	Dr.	1,32,164	5	6,60,820
30th April	To Interest A/c	364		Dr.	1,32,528	-	-

Working notes

1. **Interest from 1st April, 2015 to 15th April, 2015**

(Products for the period x rate of interest)/365

(5,00,000 x 12/100)/365 = ₹ 164

2. **Interest from 16th April, 2015 to 30th April, 2015**

(Products for the period x rate of interest)/365

(11,06,460 x 12/100)/365 = ₹ 364

9.

General Ledger Adjustment Account in Debtors Ledger

Date		Particulars	₹	Date		Particulars	₹
1.4.2015	To	Balance b/d	3,400	1.4.2015	By	Balance b/d	2,46,200
1.4.2015 to 30.4.2015	To	Debtors ledger adjustment A/c:		1.4.2015 to 30.4.2015	By	Debtors ledger adjustment A/c:	
		Sales return	21,700			Sales	9,74,900
		Cash received	8,62,100			B/R dishonoured	3,500
		Discount allowed	39,200	30.4.2015	By	Balance c/d	5,200
		B/R received	51,200				
30.4.2015	To	Balance c/d (Bal. fig.)	2,52,200				
			12,29,800				12,29,800

Debtors Ledger Adjustment A/c in General Ledger

Date		Particulars	₹	Date		Particulars	₹
1.4.15	To	Balance b/d	2,46,200	1.4.15	By	Balance b/d	3,400
1.4.2015 to 30.4.15	To	General ledger adjustment A/c:		1.4.2015 to 30.4.15	By	General ledger adjustment A/c:	
		Sales	9,74,900			Sales return	21,700
		B/R dishonoured	3,500			Cash received	8,62,100
30.4.15	To	Balance c/d	5,200	30.4.15		Discount allowed	39,200
						B/R received	51,200

				By Balance c/d (Bal.fig.)	2,52,200
		12,29,800			12,29,800

10. **Income and Expenditure Account**
for the year ended 31st March, 2015

	₹		₹
To Medicines consumed		By Prescription fees	3,30,000
Purchases 1,22,500		By Visiting fees	1,25,000
Less: Closing Stock (47,500)	75,000	By Fees from lectures	12,000
To Motor car expense (60,000 x 2/3)	40,000		
To Salaries (₹ 52,500 – ₹ 15,000)	37,500		
To Rent for clinic	30,000		
To General charges	24,500		
To Interest on loan	18,000		
To Excess of Income over expenditure	2,42,000		
	4,67,000		4,67,000

Capital Account
for the year ended 31st March, 2015

	₹		₹
To Drawings:		By Cash/bank	1,00,000
Motor car expenses	20,000	By Cash/bank (pension)	1,50,000
Household expenses	90,000	By Net income from practice	2,42,000
Marriage expenses	1,07,500	(derived from income	
To Salary of domestic servants	15,000	and expenditure a/c)	
To Household furniture	12,500		
To Balance c/d	2,47,000		
	4,92,000		4,92,000

Balance Sheet as on 31st March, 2015

Liabilities	₹	*Assets*	₹
Capital	2,47,000	Motor car	1,60,000
Loan	1,50,000	Surgical equipment	1,25,000

		Stock of medicines	47,500
		Cash at bank	55,000
		Cash in hand	9,500
	3,97,000		3,97,000

11. Statement of Affairs of Ms. Shreya as on 31.03.2014 and 31.03.2015

Liabilities	*31.03.2014* ₹	*31.03.2015* ₹	*Assets*	*31.03.2014* ₹	*31.03.2015* ₹
Capital (Balancing Figure)	1,22,150	2,27,125	Machinery & Tools	25,000	27,125
Loan	50,000	46,000	Furniture & Fixtures	50,000	54,750
Creditors	20,000	35,000	Stock	60,000	1,35,000
			Debtors	20,000	45,000
			Cash at Bank	35,000	42,500
			Cash in Hand	2,150	3,750
	1,92,150	3,08,125		1,92,150	3,08,125

Determination of Profit:	₹
Capital Balance as on 31.03.2015	2,27,125
Less: Prize won, retained in business	20,000
	2,07,125
Add: Withdrawals (₹ 1,000 x 12)	12,000
	2,19,125
Less: Capital Balance as on 31.03.2014	1,22,150
Profit for the year ended 31st March, 2015	96,975

Working Notes:

1. **Written Down Value of Machinery and Tools**

	₹
W.D.V. as on 01.04.2014	25,000
Less: Depreciation on W.D.V. @ 10% p.a.	2,500
	22,500
Add: Addition during the year on 01.07.2014	5,000
	27,500

Less: Depreciation on Addition @ 10% p.a. (5,000 x 10/100x9/12)	375
W.D.V. of Machinery & tools as on 31.03.2015	27,125

2. **Written Down Value of Furniture and Fixtures**

	₹
W.D.V. as on 01.04.2014	50,000
Less: Depreciation on W.D.V. @ 10% p.a.	5,000
	45,000
Add: Addition during the year on 01.01.2015	10,000
	55,000
Less: Depreciation on Addition @ 10% p.a. (10,000 x 10/100x3/12)	250
W.D.V. of Furniture & Fixtures as on 31.03.2015	54,750

12. Ratio of interest and amount due = $\frac{\text{Rate of interest}}{100+\text{Rate of interest}}=\frac{10}{110}=1/11$

There is no interest element in the down payment as it is paid on the date of the transaction. Instalments paid after certain period includes interest portion also. Therefore, to ascertain cash price, interest will be calculated from last instalment to first instalment as follows:

Calculation of Interest and Cash Price

No. of instalments	*Amount due at the time of instalment*	*Interest*	*Cumulative Cash price*
[1]	*[2]*	*[3]*	*(2-3) = [4]*
3rd	4,40,000	1/11 of ₹ 4,40,000 =₹ 40,000	4,00,000
2nd	8,40,000	1/11 of ₹ 8,40,000= ₹ 76,364	7,63,636
1st	12,03,636	1/11of ₹ 12,03,636= ₹ 1,09,421	10,94,215

Total cash price = ₹ 10,94,215 + 4,80,000 (down payment) =₹ 15,74,215.

13. **9% Central Government Bonds A/c in the books of Akash**

Date	*Particulars*	*Face Value*	*Interest*	*Amount*	*Date*	*Particulars*	*Face Value*	*Interest*	*Amount*
2014					2014				
Jan 01	To Balance b/d	60,000	1,350	59,000	Mar-31	By Bank A/c	-	3,150	-
Mar-01	To Bank A/c	10,000	375	10,000	Jul-01	By Bank A/c	25,000	563	25,000
Jul-01	To P & L A/c	-	-	417	Sep-30	By Bank A/c	-	2,025	-
Oct-01	To Bank A/c	7,500	-	7,350	Nov-01	By Bank A/c	15,000	112	14,850
Nov-01	To P & L A/c	-	-	100	Dec-31	By Balance c/d	37,500	844	37,017
Dec 31	To P & L A/c Transfer	-	4,969	-					
		77,500	6,694	76,867			77,500	6,694	76,867

Working Note:

Calculation of closing balance

Bonds in hand on 31.12.2014

From original holding	Face Value	Cost
(60,000 – 25,000 – 15,000)	20,000	19,667
(59,000/60,000 x 20,000)		
Purchased on 1st March	10,000	10,000
Purchased on 1st October	7,500	7,350
	37,500	37,017

14. **M/s DEF & CO.**

Memorandum Trading A/c
(1.4.14 to 13.9.14)

Particulars	*(₹)*	*Particulars*	*(₹)*
To Opening stock (Refer W.N.)	9,60,000	By Sales	45,98,200
To Purchases	35,49,900	By goods with customer	18,750
To Gross profit (25% of sales)	11,49,550	By Closing stock (bal. fig.)	10,42,500
	56,59,450		56,59,450

Computation of insurance claim

		₹
Stock on the date of fire (i.e. on 13.09.2014)		10,42,500
Less: Stock salvaged	40,000	
Agreed value of damaged stock	20,000	(60,000)
Loss of stock		9,82,500

Claim subject to average clause:

$$\text{Insurance claim} = \frac{\text{Loss of stock}}{\text{Value of stock on the date of fire}} \times \text{Amount of policy}$$

$$= 9,00,000/10,42,500 \times 9,82,500 = ₹\ 8,48,201$$

Working Notes:

1. **Calculation of original cost of the stock as on 31st March, 2014**

   Stock as on 31st March, 2014 was valued at 10% lower than cost.

   Hence, original cost of the stock would be ₹ 9,60,000 (8,64,000/90 × 100)

2. **Purchases for the period of 1.4.14 to 13.9.14**

	₹
Purchases	35,29,900
Add: purchases where goods have been received in godown although purchase invoice had not been received	60,000
Less: Purchase of machinery included in purchases	40,000
	35,49,900

3. **Sales for the period of 1.4.14 to 13.9.14**

	₹
Sales	46,93,200
Less: goods not been dispatched	70,000
Less: goods sent on approval basis but not yet confirmed	25,000
	45,98,200

4. **Goods with customer on 13.9.14**

Since no approval for sale has been received for the goods for ₹ 25,000

These should be valued at cost i.e. 25,000 – 25,000 x 25/100 = 18,750

15. **Revaluation Account**

	₹		₹
To Plant & Machinery (1,70,000 x 15%)	25,500	By Land & Building A/c	1,52,000
To Provision for Bad & Doubtful Debts (60,000 x 5%)	3,000		
To Outstanding Repairs to Building	6,000		
To A's Capital A/c (5/8)	73,438		
To B's Capital A/c (3/8)	44,062		
	1,52,000		1,52,000

Capital Accounts of Partners

	A	B	C		A	B	C
To A's Capital A/c	-	-	20,000	By Balance b/d	4,10,000	3,30,000	-
To B's Capital A/c			12,000	By Revaluation A/c	73,438	44,062	-
To B's Current A/c	-	68,062		By Profit & Loss A/c	70,000	42,000	-
To Balance c/d	6,00,000	3,60,000	2,40,000	By Bank	-	-	2,72,000
				By C's Capital A/c	20,000	12,000	-
				By A's Current A/c	26,562	-	-
	6,00,000	4,28,062	2,72,000		6,00,000	4,28,062	2,72,000

<u>Calculation of New Profit Sharing Ratio and gaining ratio:</u>

C's Share of Profit = 1/5 = 2/10

Remaining Share = 1 – 1/5 = 4/5

A's Share = 5/8 x 4/5 = 20/40 = 5/10

B's Share = 3/8 x 4/5 = 12/40 = 3/10

New Profit sharing Ratio = 5:3:2

Gaining ratio = 5:3 (same as old profit sharing ratio among old partners)

Balance sheet of AB & Co. as on 31.3.2015

Liabilities		₹	*Assets*		
Capital Accounts:			Land & Buildings		5,32,000
A	6,00,000		Plant & Machinery	1,70,000	
B	3,60,000		Less: Depreciation	25,500	1,44,500
C	2,40,000	12,00,000	Furniture		1,09,480
B's Current A/c		68,062	Stock		1,45,260
Trade Creditors		54,800	Sundry Debtors	60,000	
Outstanding Repairs to Building		6,000	*Less*: Provision	3,000	57,000
			Cash at Bank		3,14,060
			A's current A/c		26,562
		13,28,862			13,28,862

Working Note:

Required Balance of Capital Accounts

C's Capital after writing off Goodwill = 2,72,000 – 32,000 = 2,40,000

C's Share of Profit = 1/5

Thus Capital of the firm shall be = 2,40,000 x 5 = 12,00,000

A's Capital = 12,00,000 x 5/10 = 6,00,000 and

B's Capital = 12,00,000 x 3/10 = 3,60,000

16. Advantages of spreadsheet software as an accounting tool are:

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

17. (a) Accounting Standards deal with the issue of

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

(ii) Measurement of these transactions and events,

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

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

(b) Para 17 of AS 1 'Disclosure of Accounting Policies' recognizes 'prudence' as one of the major considerations governing the selection and application of accounting policies. In view of the uncertainty attached to future events, profits are not anticipated but recognized only when realized though not necessarily in cash. Provision is made for all known liabilities and losses even though the amount cannot be determined with certainty and represents only a best estimate in the light of available information. Also as per para 10 of the AS 1, 'accrual' is one of the fundamental accounting assumptions. Irrespective of the terms of the contract, so long as the principal amount of a loan is not repaid, the lender cannot be replaced in a disadvantageous position for non-payment of interest in respect of overdue amount. From the aforesaid, it is apparent that the company has an obligation on account of the overdue interest. In this situation, the company should provide for the liability (since it is not waived by the lenders) at an amount estimated or on reasonable basis based on facts and circumstances of each case. However, in respect of the overdue interest amounts, which are settled, the liability should be accrued to the extent of amounts settled. Non-provision of the overdue interest liability amounts to violation of accrual basis of accounting. Therefore, the treatment, done by the company, of not providing the interest amount from due date to the date of repayment is not correct.

18. (a) Net Realisable Value of Inventory as on 31st March, 2015

= ₹ 107.75 x 20 units = ₹ 2,155

Value of inventory as per Weighted Average basis

<u>Total units purchased and total cost:</u>

01.03.2015	₹ 108 x 20 units = ₹ 2160
08.3.2015	₹ 107 x 15 units = ₹ 1605
17.03.2015	₹ 109 x 30 units = ₹ 3270
25.03.2015	₹ 107 x 15 units = ₹ 1605
Total	80 units = ₹ 8640

Weighted Average Cost = ₹ 8640/80 units = ₹108

Total Value = ₹ 108 x 20 units = ₹ 2,160

Value of inventory to be considered while preparing Balance Sheet as on 31st March, 2015 is, Cost or Net Realisable value whichever is lower i.e. ₹ 2,155.

(b) **(i)** Operating Activities: c, e, f, g, j, m, o, s, t, w, x, aa & gg.

(ii) Investing Activities: a, h, k, l, p, q, u, v, bb & ee.

(iii) Financing Activities: b, d, i, n, r, y, z, cc & dd.

(iv) Cash Equivalent: ff.

19. **(a)** Depreciation per year = ₹ 1,20,000 / 10 = ₹ 12,000

Depreciation on SLM charged for three years = ₹ 12,000 x 3 years = ₹ 36,000

Book value of the computer at the end of third year = ₹ 1,20,000 – ₹ 36,000

= ₹ 84,000.

Remaining useful life as per previous estimate = 7 years

Remaining useful life as per revised estimate = 5 years

Depreciation from the fourth year onwards = ₹ 84,000 / 5 = ₹ 16,800 per annum

(b) Total expected loss to be provided for Contract Price –Total Cost

= ₹ 50,00,000 –(21,00,000 + 31,50,000) = ₹ 2,50,000

Calculation for 2014-15 on 40% work

Contract Revenue	= ₹ 21,00,000
Contract Cost	= ₹ 21,00,000
Loss on contract	= ₹ 1,00,000
Expected loss recognized as per AS 7	= ₹ 2,50,000
Further provision required in respect of	
Expected Loss (₹2,50,000 - ₹1,00,000)	= ₹ 1,50,000

In the Books of Five Star construction Limited

Profit & Loss A/c (Extract) for the year ended 31st March 2015

	Amount (₹)		*Amount (₹)*
To Construction Costs (for 40% work)	21,00,000	By Contract Revenue	20,00,000
To Provision for Loss	1,50,000	By Net Loss	2,50,000
	22,50,000		22,50,000

20. (a) As per AS 9, "Revenue Recognition" is the inflow of cash, receivable or other consideration arising in the course of ordinary activities of an enterprise from the sale of Goods. However, the above is subject to trade discount and volume rebates received in the course of carrying on business which shall be deducted in ascertaining revenue since they represent a reduction of cost. Revenue is also subject to certain risks like damages on transfer of goods to the buyers' end.

In the given case, trade discount is to be deducted from ₹ 13,00,000 and gross sale shall be recognized at (₹ 13,00,000 - ₹ 1,06,000) = ₹ 11,94,000 and goods returned ₹ 1,34,000 are to be recorded in the form of sales return.

Thus the contention of the Accountant to book sale of ₹ 10,60,000 is not correct.

(b) Calculation of cost of fixed asset

	₹
Materials	10,00,000
Direct labour (1/6th of ₹ 3,00,000)	50,000
Direct expenses	2,00,000
Office and administrative expenses (5% ₹ 7,50,000)	37,500
Depreciation on assets	10,000
Total Cost of fixed asset	12,97,500

PAPER – 2: BUSINESS LAWS, ETHICS & COMMUNICATION

PART – I: ANNOUNCEMENTS STATING APPLICABILITY & NON-APPLICABILITY FOR MAY, 2016 EXAMINATION

I. Applicability for May 2016 examinations

Applicability of relevant amendments/Circulars/Notifications/Regulations etc. for the period 1st May 2015 to 31st October, 2015 relating to Business Law, Ethics and Communication at Intermediate (IPC) for May 2016, Examination:

(i) The Companies Act, 2013

Sl. No.	Amendment related to the topic	Content
1	The Companies (Acceptance of Deposits) Second Amendment Rules, 2015	Vide Notification No. G.S.R. 695(E) dated 15th September 2015, the Ministry of Corporate Affairs makes the Companies (Acceptance of Deposits) Second Amendment Rules, 2015 further to amend the Companies (Acceptance of Deposits) Rules, 2014. This amendment has substituted sub-clause (viii) of clause (c), sub-rule (1), rule 2.
2	The Companies (Management and Administration) Amendment Rules, 2015.	Vide Notification No. G.S.R. 669(E) dated 28th August 2015, the MCA makes the Companies (Management and Administration) Amendment Rules, 2015 further to amend the Companies (Management and Administration) Rules, 2014. Through this amendment, rule 23, in sub-rule (l) for the words 'not more than five lakh rupees", the words 'not less than five lakh rupees' shall be substituted.
3	Exemptions to companies covered under section 8	Vide Notification G.S.R. 466(E) dated 5th June 2015, the Central Government in the interest of public, hereby directs that certain provisions of the Companies Act, 2013, shall not apply or shall apply with certain exceptions, modifications and adaptations to a body to which a license is granted under the section 8 of the Act.
4	Exemptions to private companies	Vide Notification no. G.S.R. 464(E), dated 5th June 2015 the Central Government in the interest of public, hereby directs that certain provisions of the Companies Act, 2013, shall not apply or shall apply with certain exceptions, modifications and adaptations to a private company.

5	Exemptions to Nidhi companies	Vide Notification G.S.R. 465(E) dated 5 June 2015 the Central Government hereby directs that certain provisions of the Companies Act, 2013, shall not apply or shall apply with such exceptions, modifications and adaptations to Nidhis.
6	Exemptions to Government Companies	Vide Notification dated G.S.R.463(E) dated 5 June 2015 the Central Government hereby directs that certain provisions of the Companies Act, 2013, shall not apply or shall apply with such exceptions, modifications and adaptations to a Government company.
7	The Companies (Amendment) Act, 2015	Vide Notification dated 29th May 2015, Central Government declared the date of enforcement of provisions of sections 1 to 12 and 15 to 23 of the Companies (Amendment) Act, 2015.
8	Delegation of power and functions to Regional Directors under section 94 (5) of the Companies Act, 2013	In exercise of the powers conferred by Section 458 of the Companies Act, 2013 (18 of 20l3), the Central Government hereby delegates to the Regional Directors at Mumbai, Kolkata, Chennai, Noida, Ahmedabed, Hyderabad and Shillong the powers and functions vested in it under sub-section (5) of Section 94 of the Companies Act, 2013, subject to the condition that the Central Government may revoke such delegation of powers or may itself exercise the powers under the said sub-section, it in its opinion such a course of action h necessary in the public interest.

(ii) The Negotiable Instruments (Amendment) Second Ordinance, 2015 : In exercise of the powers conferred by Article123(1) of the Constitution, the President promulgated the ordinance called the Negotiable Instruments(Amendment) Second Ordinance, 2015 with effect from 15th June, 2015. Amendments is made with an object to address the difficulties faced by the payee or the lender of the money in filing cases under section 138 of the said Act, because of which large, large number of cases are stuck, so the jurisdiction for offence under section 138 has been clearly defined. For detail click the following link-

http://www.prsindia.org/uploads/media/Negotiable%20instrument/Negotiable%20Instruments%20(A)%20second%20Ordinance.pdf

Students are advised to refer the study material (July 2015 edition) along with the practice manual (July 2015 edition).

II. Non-Applicability for May 2016 examinations

S.No.	Section No.	Section title
1.	Section 48	Variation of shareholders' right
2.	Section 66	Reduction of share capital
3.	Section 75	damages for fraud
4.	Section 97	Power of tribunal to call AGM
5.	Section 98	Power of Tribunal to call meetings of members, Etc.
6.	Section 99	Punishment for default in complying with provisions of sections 96 to 98

PART – II : QUESTIONS AND ANSWERS

QUESTIONS

PART – A: BUSINESS LAWS

The Indian Contract Act, 1872

1. (a) Vishal, aged 16 years, was studying in an engineering college. On 1 March, 2013 he took a loan of ₹ 1 lakh from Shekhar for the payment of his college fee and agreed to pay by 30th May, 2014. Vishal possesses assets worth ₹ 10 lakhs. On due date Vishal fails to pay back the loan to Shekhar. Shekhar now wants to recover the loan from Vishal out of his assets. Whether Shekhar would succeed? Decide, referring to the provisions of the Indian Contract Act, 1872.

   (b) What is the meaning of the term 'Reciprocal Promise'. In what forms the performance of reciprocal promise can take place according to the provision of the Indian Contract Act, 1872.

2. (a) Father promised to pay his son a sum of rupees one lakh if the son passed C.A. examination in the first attempt. The son passed the examination in the first attempt, but father failed to pay the amount as promised. Son files a suit for recovery of the amount. State along with reasons whether son can recover the amount under the Indian Contract Act, 1872?

   (b) Mr. Yadav of Delhi engaged Mr. Shekhawat as his agent to buy a house in West Extension area. Mr. Shekhawat bought a house for ₹ 50 lakhs in the name of a nominee and then purchased it himself for ₹ 60 lakhs. He then sold the same house to Mr. Yadav for ₹ 62 lakhs. Mr. Yadav later comes to know the mischief of Mr. Shekhawat and tries to recover the excess amount paid to Mr. Shekhawat. Is he entitled to recover any amount from Mr. Shekhawat? If so, how much? Explain.

The Negotiable Instruments Act, 1881

3. Ram, a legal successor of Shyam, the deceased person, signs a Bill of Exchange in his own name admitted a liability of ₹ 1,50,000 i.e. the extent to which he inherits the assets from the deceased payable to Mohan after 3 months from 1st January, 2015. On maturity, when Mohan presents the bill to Ram, he (Ram) refuses to pay for the bill on the ground that since the original liability was that of Shyam, the deceased, therefore he is not liable to pay for the bill.

   Referring to the provisions of the Negotiable Instruments Act, 1881 decide whether Mohan can succeed in recovering ₹ 1,50,000 from Ram.

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

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

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

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

The Payment of Bonus Act, 1965

5. Referring the provisions of the Payment of Bonus Act, 1965, state whether the following persons are entitled to bonus under the Act:

   (i) An apprentice;

   (ii) An employee dismissed on the ground of misconduct;

   (iii) A temporary workman;

   (iv) A piece-rated worker;

   (v) An employee getting a salary of ₹ 12,000 per month.

6. Precious Wooden Toys Limited was established at Kolkota in the year 2012 employing 100 workmen. Since then, the company suffered losses, but minimum bonus was paid in the accounting years of 2013 and 2014. In the accounting year 2015, the company earned huge profits. After mitigating the previous losses the company is having surplus profits and wants to pay the bonus to its workmen. Precious Wooden Toys Limited wants legal advice on the following issues:

   (a) How much minimum and maximum bonus may be paid to the workmen?

   (b) Whether the company may adjust the puja bonus already paid to the workmen while calculating the amount of bonus payable to workmen for that accounting year.

   (c) Company wants to give wooden toys as bonus instead of cash. Whether the company can do so?

   Advise Precious Wooden Toys Limited, stating the provisions of the Payment of Bonus Act, 1965.

The Employees' Provident Funds and Miscellaneous Provisions Act, 1952

7. 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. X, an employee in ABC Ltd (covered by the EPF and MP Act, 1952) died in an accident. State to whom the amount standing in his account to be payable under the provisions of the Act.

The Payment of Gratuity Act, 1972

9. Examine the validity of the following nominations in respect of payment of gratuity as per the provisions of the Payment of Gratuity Act, 1972. Also specify the provisions in this reference:

   (i) 'R' who has 4 members in his family wants to nominate one of his friend for the purpose of gratuity.

   (ii) 'S' who has no family, nominated one of his friend for the purpose of gratuity. Afterwards he acquired family but did not change the nomination.

10. An employee who is governed by the Payment of Gratuity Act, 1972 committed a theft in the course of his employment. And consequently his services was terminated. State in this connection, whether the gratuity payable to him shall be wholly or partly forfeited.

The Companies Act, 2013

11. Sujeev, a shareholder, holding 2000 shares of ₹ 100 per share of Touchwood Pharma Ltd. The company has called and collected ₹ 60 per share. Sujeev has paid ₹ 40 per share (the balance amount not yet demanded by the company) as calls in advance. At the time of annual general meeting of the company, he demanded that he is entitled to vote in respect of the advance money paid by him. The directors of the company rejected his demand. He claimed for refund of calls in advance amount paid by him with interest.

    Examine the validity of Sujeev's claim for voting or refund of money with interest with reference to the provisions of the Companies Act, 2013.

12. Lotus valley Ltd. issued a prospectus with the object of setting up of a chain of hotels. However, later it decided to set-up a Pharmaceutical Manufacturing unit. Keeping in view of the provisions of the Companies Act, 2013, state whether Lotus valley Ltd. can do so and if it can be done, also state the procedure to be followed for variation in the objects in the prospectus.

13. Can a non-profit organization be registered as a company under the Companies Act, 2013? If so, what procedure does it have to adopt?

14. ADJ Limited decides to buy-back its own shares. Advise the company's Board of Directors about the sources out of which the company can buy-back its own shares.

What conditions are attached to the buy-back scheme of the company in accordance with the provisions of the Companies Act, 2013? Explain.

15. Examine the validity of the following decisions of the Board of Directors with reference of the provisions of the Companies Act, 2013.
    (i) In an Annual General Meeting of a company having share capital, 80 members present in person or by proxy holding more than $1/10^{th}$ of the total voting power, demanded for poll. The chairman of the meeting rejected the request on the ground that only the members present in person can demand for poll.
    (ii) In an annual general meeting, during the process of poll, the members who earlier demanded for poll want to withdraw it. The chairman of the meeting rejected the request on the ground that once poll started, it cannot be withdrawn.

PART – B: ETHICS

16. "To pay proper attention to business ethics is certainly beneficial in the interest of business. Describe four such benefits which may be obtained by paying attention to business ethics.
17. What is Corporate Social Responsibility? Why it is needed in Indian Business environment?
18. What do you understand by the term 'discrimination' in employment as sometime found in an establishment? Explain the basic elements of 'discrimination'.
19. (i) What is meant by 'Environmental ethics'? How does its non-adoption lead to 3 Ps Viz., Polluter Pays and Principles? Explain.
    (ii) What are the objects of the "Central Consumer Protection Council" in relation to protection of rights of the consumers?
20. What are the fundamental principles of ethics applicable to the persons of finance and accounting profession?

PART – C: COMMUNICATION

21. What are the factors that lead to grapevine communication?
22. What do you understand by 'Group conflicts'? How shall these be managed effectively? Explain.
23. State the reasons for accepting the change in the present management set-up of the corporate culture in a business organisation.
24. Mr. Somnath has not received a dividend warrant of ₹ 1,700 for 170 shares of Cute Fabrics Ltd. Draft an indemnity bond, to be given to the company for seeing release of Dividend.

25. Ashoka Paper Limited was incorporated in September, 2015. Now the company wants to hold its first meeting of the Board of Directors. Draft a notice of the said meeting along with agenda.

SUGGESTED ANSWERS/HINTS

1. (a) According to Section 11 of the Indian Contract Act, 1872, a person who is of the age of majority to the law to which he is subject is competent to enter into any contract. A person who has completed the age of 18 years is a major and otherwise he will be treated as minor. Thus, Vishal who is a minor is incompetent to contract and any agreement with him is void *[Mohori Bibi Vs Dharmodas Ghose 1903, 30 Cal, 539 (PC)].*

Section 68 of the Indian Contract Act, 1872 however, prescribes the liability of a minor for the supply of the things which are the necessaries of life to him. It says that though minor is not personally liable to pay the price of necessaries supplied to him or money lent for the purpose, the supplier or lender will be entitled to claim the money/price of goods or services which are necessaries suited to his condition of life provided that the minor has a property. The liability of minor is only to the extent of the minor's property. This type of contract is called a Quasi-contract and the right of the supplier/lender is based on the principle of equity.

Thus, according to the above provision, Shekhar will be entitled to recover the amount of loan given to Vishal for payment of the college fees from the property of the minor.

(b) The law relating to reciprocal promise are set out in Sections 51 to 54 of the Indian Contract Act, 1872.

General observation: A contract may consist of (i) an act and a promise or (ii) two promises one being the consideration for the other.

The second type of contract which involves two promises, one promise from each to the other party is known as "Reciprocal promise".

The performance of reciprocal promise can take in different forms-

(i) **Simultaneously performance of reciprocal promise [Section 51]:** In this case, promises have to be performed simultaneously. The conditions and performances are concurrent. If one of the parties does not perform his promise, the other also need not perform his promise.

(ii) **Performance of reciprocal promise where the order is expressly fixed:** Where the order of performance is expressly fixed, the promise must be performed in that order only.

(iii) Performance of reciprocal promise by implication: Where the performance of reciprocal promise is not fixed expressly, some times the order is understood by implication.

(iv) Effect of one party preventing another from performing promise [Section 53]: When in a contract consisting of reciprocal promises one party prevents the other from performing his promise, the contract becomes voidable at the option of the party so prevented. The person so prevented is entitled to get compensation for any loss he may have sustained for the non-performance.

(v) Effects of default as to promise to be performed first: Section 54 of the Act provides that promises may be such that:

(A) one of them cannot be performed or

(B) its performance cannot be demanded till the other has been performed.

(vi) Position of legal and illegal parts of Reciprocal promises: Reciprocal promise to do certain things that are legal and certain others that are not legal –

Section 57 of the Act provides that if reciprocal promises have two parts, the first part being legal and the second part being illegal, the legal part is a valid contract and the illegal part is void.

(vii) Alternative promise one branch being illegal: "In the case of the alternative promise, one branch of which is legal and the other illegal, the legal branch alone can be enforced".

2. (a) Problem asked in the question is based on the provisions of the Indian Contract Act, 1872 as contained in section 10. According to the provisions, there should be an intention to create legal relationship between the parties. Agreements of a social nature or domestic nature do not contemplate legal relationship and as such are not contracts, which can be enforced. This principle has been laid down in the case of *Balfour vs. Balfour (1912 2 KB. 571).* Accordingly, applying the above provisions and the case decision, son cannot recover the amount of ` 1 lakh from father for the reasons explained above.

(b) The problem in this case, is based on the provisions of the Indian Contract Act, 1872 as contained in Section 215 read with Section 216. The two sections provide that where an agent without the knowledge of the principal, deals in the business of agency on his own account, the principal may:

(1) repudiate the transaction, if the case shows, either that the agent has dishonestly concealed any material fact from him, or that the dealings of the agent have been disadvantageous to him.

(2) claim from the agent any benefit, which may have resulted to him from the transaction.

Therefore, based on the above provisions, Mr. Yadav is entitled to recover ₹ 12 lakhs from Mr. Shekhawat being the amount of profit earned by Mr. Shekhawat out of the transaction.

3. The problem is based on the provisions of the Negotiable Instruments Act, 1881 as contained in Section 29. A legal representative of a deceased person who signs his own name on a negotiable instrument, is personally liable for the entire amount thereon, unless he expressly limits his liability to the extent of the assets received by him as such (Section 29).

   Applying the above provisions to the given problem *Mohan* is entitled to recover ₹ 1,50,000/- from Ram. Ram cannot refuse to pay the amount since he has inherited the assets of the deceased. He will be liable to the extent of the full amount of the bill even if he inherits the property valued less than the amount of the bill. Thus, in this case he will be liable to full amount of ₹ 1,50,000/-.

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

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

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

5. **(i)** An Apprentice is not entitled to bonus within the meaning of "Employee" under section 2(13) of the Payment of Bonus Act, 1965 and as also decided in the case *[Wheel RIM Co. Vs. Govt. of Tamil Nadu (1971)]*

   (ii) An employee dismissed on the ground of misconduct shall be disqualified for any bonus under section 9 of the Payment of Bonus Act, 1965 only if the misconduct falls within the meaning of:

(a) Fraud; or

(b) Riotous or violent behaviour while on the premises of the establishment; or

(c) Theft, misappropriation or sabotage of any property of the establishment.

It may be noted from the above grounds of disqualification, that "misconduct" is not mentioned. Misconduct is a broad term and can be interpreted to mean many things such as "insubordination", "misbehavior" or even "deliberate sub standard performance or negligence", but none of these will disqualify an employee from receiving bonus. Therefore, an employee dismissed on the ground of misconduct will be disqualified only if the conditions in a, b or c above can be established. *[Pandian Roadways Corporation Ltd. Vs. Presiding Officer (1996)]*

(iii) A temporary workman is entitled to bonus on the basis of the total number of days worked by him.

(iv) A piece-rated worker is entitled to bonus. *[Mathuradas Kanji Vs. L.A. Tribunal (1958)]*

(v) Under section 2 (13) of the payment of Bonus Act, 1965 a person drawing a monthly salary of an amount in excess of ₹ 10,000, shall not fall within the meaning of an employee and consequently not eligible to receive bonus under the Act.

6. **Payment of bonus:** In accordance with the provisions of Section 10 of the Payment of Bonus Act, 1965, every employer shall be bound to pay to every employee in respect of any accounting year, a minimum bonus which shall be 8.33 percent of the salary or wage earned by the employee during the accounting year or hundred rupees, whichever is higher, whether or not the employer has any allocable surplus in the accounting year. Therefore, even in the case of loss, the minimum bonus has to be paid.

Further, in accordance with the provisions of Section 11(1) the maximum bonus payable to an employee is 20% of the salary or wage earned by him in any accounting year. Bonus at a rate higher than the minimum bonus of 8.33% is payable only when the allocable surplus computed in accordance with the provisions of the Payment of Bonus Act, 1965 exceeds the amount of minimum bonus payable subject to the maximum limit of 20%.

Section 17 of the Act provides for the adjustment of any customary or puja bonus or any advance bonus against the bonus payable under this Act for an accounting year and pay only the balance bonus after such deduction / adjustment to the employee.

Bonus should be paid only in cash by the employer.

The legal advice in the given case may be given on the basis of the provisions of the Act accordingly:

(a) **As regards minimum and maximum bonus:** The company has surplus profits after setting off past losses. It appears therefore, that the allocable surplus is higher than the minimum bonus payable under the Act which is 8.33%. Hence, the company is bound to pay bonus at a rate higher than the minimum bonus rate but upto a maximum of 20%. Therefore, Precious Wooden Toys Ltd is bound to pay bonus at a rate higher than 8.33% depending on its allocable surplus but upto a maximum of 20%.

(b) **As regards adjustment of Puja Bonus:** In accordance with the provisions of Section 17 of the Payment of Bonus Act, 1965 where, in an accounting year an employer has paid any puja bonus or other customary bonus to an employee, the employer shall be entitled to deduct (adjust) the amount of bonus so paid from the amount of bonus payable to the employee in respect of that accounting year and the employee shall be entitled to receive only the balance. Therefore, Precious Wooden Toys Ltd. may adjust the puja bonus already paid from the amount of bonus payable to the workmen and the workmen shall be entitled to receive only the balance.

(c) The amount payable to an employee by way of bonus under the Payment of Bonus Act, 1965, shall be paid only in cash by the employer. Therefore, Precious Wooden Toys Ltd. cannot distribute wooden toys, instead of cash, as bonus. It is against the statutory provisions.

7. **Contribution to Provident Fund under the EPF and Miscellaneous Provisions Act, 1952:** Section 6 of the EPF and MP Act, 1952 regulates contribution to Provident Fund Scheme established under the Act.

The employer's contribution shall be 10% of the basic wages, dearness allowance and retaining allowance, if any payable to each of the employees whether employed by him directly or by or through a contractor.

The employee's contribution shall be equal to the contribution payable by the employer in respect of him.

In case the employee so desires, he may contribute an amount exceeding ten percent of his basic wages, dearness allowance and retaining allowance if any, subject to the condition that the employer shall not be under an obligation to pay any contribution over and above his contribution payable under this section.

Dearness allowance includes cash value of any food concession allowed to the employees. Retaining allowance means the sum paid for retaining the service, when the factory is not working.

The Central Government may by notification make the employer's contribution equal to 12% for certain class of establishments.

8. As per Section 10 of the Employees' Provident Funds and Miscellaneous Provisions Act, 1952, the amount standing to the credit of any member in the fund or of any exempted employee in a provident fund shall not in any way be capable of being assigned or charged and shall not be liable to attachment under any decree or order of any court in respect of any debt or liability incurred by the member or exempted employee, and

neither the official assignee appointed under the Presidency Town Insolvency Act, 1909, nor any receiver appointed under the Provincial Insolvency Act, 1920, shall be entitled to or have any claim on, any such amount. This protection also applies to provident fund, pension and insurance amount receivable by employee under the scheme.

The amount standing to the credit of the person at the time of his death is payable to his nominees under the scheme or the rules under this Act.

Further, the amount shall be free from any debt or other liability incurred by the deceased or the nominee before the death of the member or of the exempted employee and shall also not be liable to attachment under any decree or order of any Court.

9. The provisions regarding nomination of gratuity under the Gratuity Act, 1972 are as below:

(i) **Nomination in favour of one or more family members**: If an employee has a family at the time of making a nomination, the nomination shall be made in favour of one or more members of his family, and any nomination made by such employee in favour of a person who is not a member of his family shall be void. Therefore, the nomination of friend by R in the above case is void.

(ii) **Nomination by the employee having no family/ subsequently acquiring family**: If at the time of making a nomination the employee has no family, the nomination may be made in favour of any person or persons but if the employee subsequently acquires a family, such nomination shall forthwith become invalid and the employee shall make, within such time as may be prescribed, a fresh nomination in favour of one or more members of his family. Therefore, the nomination in the above case by 'S' is also void. He has to nominate from his family members for the purpose of gratuity.

10. **Reduction and forfeiture of Gratuity**: Under Section 4 (6)(a) of the Payment of Gratuity Act, 1972, in the case of damage, loss or destruction of property of employer, due to the willful omission or negligence of the employee, the amount of gratuity to the extent of loss or damage shall be forfeited by the employer.

Further, under section 4(6)(b), the gratuity payable to an employee may be wholly or partially forfeited, where the services of an employee are terminated on the ground of:

(i) riotous or disorderly conduct or act of violence; or

(ii) committing an offence involving moral turpitude in the course of his employment.

Theft is an offence involving moral turpitude and consequently, if the services of an employee had been terminated for committing theft in the course of his employment, the gratuity payable to him under the provisions of the Act shall be wholly forfeited in view of Section 4(6)(b)(ii). *[Bharat Gold Mines Ltd. Vs Regional Labour Commissioner (Central), (1987) 70 FJR 11 (Kern.)]*]

11. According to Section 50 of the Companies Act, 2013, a company may, if so authorized by the Articles, accept from any member, the whole or a part of the amount remaining unpaid on any shares by him, even if no part of that amount has been called up. The amount so received or accepted is described as payment in advance of calls. When a company receives payment in advance of calls, the consequences will be as follows:

(i) The shareholder is not entitled to voting rights in respect of the moneys so paid by him until the same would, but for such payment, become presently payable [Section 50)].

(ii) The shareholder's liability to the company in respect of the call for which the amount is paid is extinguished.

(iii) The shareholder is entitled to claim interest on the amount of the call to the extent payable according to articles of association. If there are no profits, it must be paid out of capital, because shareholder becomes the creditor of the company in respect of this amount.

(iv) The amount received in advance of calls is not refundable.

(v) In the event of winding up, the shareholder ranks after the creditors, but must be paid his amount with interest, if any, before the other shareholders are paid off.

(vi) The power to receive the payment in advance of calls must be exercised in the general interest and for the benefit of the company. (*syke's case (1872) L.R. 13 Eq. 255*)

Therefore, according to the above provisions:-

(i) Sujeev is not entitled to vote in respect of the moneys so paid by him until the same would, but for such payment, become presently payable.

(ii) As per the provisions of law, the amount received in advance of calls is not refundable. However, Sujeev is entitled to claim interest on the amount of the call to the extent payable according to the Articles of Association. If there are no profits, it must be paid out of capital, because shareholder becomes the creditor of the company in respect of this amount.

12. As per Section 27 of the Companies Act, 2013, Lotus valley Ltd. can change the object mentioned in the prospectus. Section 27 of the Companies Act, 2013 deals with variation in the terms of contract or objects in the prospectus.

To change the object mentioned in the prospectus, Lotus valley Ltd. has to follow the under mentioned procedure:-

(1) **Vary by special resolution:** A company shall not, at any time, vary the terms of a contract referred to in the prospectus or objects for which the prospectus was issued, except by way of special resolution.

(2) **Notice of resolution to shareholders:** The details of the notice in respect of such resolution to shareholders, shall also be published in the newspapers (one in English and one in vernacular language) in the city where the registered office of

the company is situated indicating clearly the justification for such variation. Also that such company shall not use any amount raised by it through prospectus for buying, trading or otherwise dealing in equity shares of any other listed company.

(3) **Exit offer to dissenting shareholders:** The dissenting shareholders being those shareholders who have not agreed to the proposal to vary the terms of contracts or objects referred to in the prospectus, shall be given an exit offer by promoters or controlling shareholders at such exit price, and in such manner and conditions as may be specified by the Securities and Exchange board by making regulations in this behalf.

Thus Lotus valley Ltd. can change the object mentioned in the prospectus from setting up a chain of hotels to setting up of a pharmaceutical manufacturing unit by following the above mentioned procedure.

13. Registration of a non-profit organisation as a company: According to section 8 (1) of the Companies Act, 2013, the Central Government may allow person or an association of persons to be registered as a Company under the Companies Act if it has been set up for promoting commerce, arts, science, sports, education, research, social welfare religion, charity, protection of environment or any such other useful object and intends to apply its profits or other income in promotion of its objects. However, such company has to prohibit payment of any dividend to its members.

Procedure: An association of persons intending to carry any or all or some of the activities mentioned in section 8 (1) as mentioned above, has to apply to the Central Government seeking its permission for being set up as a company under the Act. The central government if satisfied on the above may by the issue of a licence in such manner as may be prescribed and on such conditions as it may deem fit, allow such association to be registered as a limited company under section 8 (1) without the addition of word "Limited" or words "Private Limited" as the case may be, to its name.

After the issue of the licence by the Central Government, an application must be made to the Registrar in the prescribe form after which the Registrar will register the association of persons as a company under section 8(1). Under section 8 (2) a company registered under section 8 (1) as above, shall enjoy all the privileges and be subject to all the obligations of a limited company.

This licence issued by the Central Government is revocable, and on revocation the Registrar shall put the words 'Limited' or 'Private Limited' against the company's name in the Register. But before such revocation, the Central Government must give the company a written notice of its intention to revoke the licence and provide an opportunity to it to be represented and heard in the matter.

[**Note:** *As per the Notification S.O. 1353(E), dated 9th of July, 2014, the Central Government. hereby delegates to the ROC the power & functions vested in it under the section 8(1) of the Companies Act, 2013, subject to the condition that the Central*

Government may revoke such delegation of powers or may itself exercise the powers & functions under the said sections, if in its opinion, such course of action is necessary in the public interest.]

14. Sources of funds for buy-back of shares: Under section 68 (1) of the Companies Act, 2013 a company can purchase its own shares or other specified securities. The purchase should be out of:

(i) its free reserves; or

(ii) the securities premium account; or

(iii) the proceeds of the issue of any shares or other specified securities.

However, buy-back of any kind of shares or other specified securities cannot be made out of the proceeds of an earlier issue of the same kind of shares or same kind of other specified securities.

'Specified securities' includes employees' stock option or other securities as may be notified by the Central Government from time to time. [Explanation (1) under Section 68],

Requirements to be complied with before buy-back: Under section 68 (2) of the Companies Act, 2013 a company shall not purchase its own shares or other specified securities unless:

(a) the buy-back is authorised by its articles;

(b) a special resolution (also Declaration of Solvency to be filed with ROC & SEBI in case shares are listed on any recognised stock exchange), authorising the buy-back is passed at a general meeting of the company;

(c) the buy-back is 25% or less than of the aggregate of the paid-up capital and free reserves of the company;

Provided that the buy-back of equity shares in any financial year shall not exceed 25% of its total paid up equity capital in that financial year.

(d) the ratio of the aggregate of the secured and unsecured debt owed by the company is not more than twice the capital and free reserves after such buy-back;

Provided that the Central Government may prescribe a higher ratio of the debt than that specified under this clause for a class or classes of companies. The second explanation to section 68 clarifies that the expression "free reserves" shall include the securities premium account.

(e) all the shares or other specified securities for buy-back are fully paid-up;

(f) the buy-back of the shares or other specified securities listed on any recognised stock exchange is in accordance with the regulations made by SEBI in this behalf;

(g) the buy-back in respect of shares or other specified securities other than those specified in Clause (f) above is in accordance with such guidelines as may be prescribed.

Under section 68 (3) of the Companies Act, 2013 the notice of the meeting at which the special resolution is proposed to be passed shall be accompanied by an explanatory statement stating;

(a) a full and complete disclosure of all material facts;

(b) the necessity for the buy-back;

(c) the class of shares or securities intended to be purchased under the buy- back;

(d) the amount to be involved under the buy-back; and

(e) the time limit for completion of buy-back.

Under section 68 (4) of the Companies Act, 2013 every buy back must be completed within a period of one year from the date of the passing of the special resolution, or the Board Resolution where the buy back is upto 10% of the aggregate of the paid up capital and free reserves of the company.

Under section 68 (5) a company proposing to buy back its own shares must file with the Registrar and with SEBI a declaration of solvency signed by at least two directors out of which one must be the Managing Director. This must be filed before proceeding with the buy back.

Requirements to be complied with after buy-back:

(1) The securities bought back should be extinguished and physically destroyed within 7 days after completion of buy-back [Section 68 (7)].

(2) After completion of buy-back, a company cannot issue same kind of shares or security (which was bought back) for a period of 6 months. Allotment of rights issue renounced by members is also not permissible in this period. However, following are permitted:

    (i) issue of security of a different class that is other than one which was bought back,

    (ii) bonus issue,

    (iii) subsisting obligations such as conversion of warrants,

    (iv) stock option to employees

    (v) sweat equity

    (vi) conversion of preference shares or debentures into equity shares [Section 68(8)].

(3) The company should maintain a register showing securities bought back and consideration paid for the buy-back, date of cancellation of securities, date of extinguishment and physical destruction of securities and such other prescribed particulars [Section 68(9)].

(4) After completion of buy-back, a return has to be filed with the Registrar of Companies and Securities and Exchange Board of India if the company is listed within 30 days giving details as prescribed [Section 68(10)].

(5) If the buy-back is from free reserves, a sum equal to the nominal value of shares purchased will be transferred to capital redemption reserve account. Details of such transfer will be disclosed in the balance sheet of the company [(Section 69 (1)].

15. Section 109 of the Companies Act, 2013 provides for the demand of poll before or on the declaration of the result of the voting on any resolution on show of hands. Accordingly law says that:-

Order of demand for poll by the chairman of meeting: Before or on the declaration of the result of the voting on any resolution on show of hands, a poll may be ordered to be taken by the Chairman of the meeting on his own motion, and shall be ordered to be taken by him on a demand made in that behalf:-

(a) In the case a company having a share capital, by the members present in person or by proxy, where allowed, and having not less than one-tenth of the total voting power or holding shares on which an aggregate sum of not less than five lakh rupees or such higher amount as may be prescribed has been paid-up; and

(b) in the case of any other company, by any member or members present in person or by proxy, where allowed, and having not less than one tenth of the total voting power.

Withdrawal of the demand: The demand for a poll may be withdrawn at any time by the persons who made the demand.

Hence, on the basis on the above provisions of the Companies Act, 2013:

(i) The chairman cannot reject the demand for poll subject to provision in the articles of company.

(ii) The chairman cannot reject the request of the members for withdrawing the demand of the Poll.

16. **Benefits which may be obtained by paying attention to business ethics:** Ethics is the concern for good behaviour – doing the right thing. In business, self interest prevails and there is always inconsistency between ethics and business. But it is a well settled principle that ethical behaviour creates a positive reputation that expands the opportunities for profit. The awareness regarding products and services of an organization, and the actions of its employees can affect its stakeholders and society as a whole. Therefore, to pay proper attention to business ethics may be beneficial in the interest of business. These benefits may be enumerated as follows:

(1) In the recent past ruthless exploitation of children and workers, trust control over the market, termination of employees based on personalities and other factors had affected society and a demand arose to place a high value on ethics, fairness and equal rights resulting in framing of anti-trust laws, establishment of governmental agencies and recognition of labour unions.

(2) Easier change management: Attention to business ethics is also critical during times of fundamental change. The apparent dilemma may be whether to be non profit or for profit. In such situations, often there is no clear moral compass to guide leaders about what is right or wrong. Continuing attention to ethics in the workplace sensitises leaders and staff for maintaining consistency in their actions.

(3) Strong team work and greater productivity: Ongoing attention and dialogues regarding ethical values in the workplace builds openness, integrity and a sense of community which leads to, among the employees, a strong alignment between their values and those of the organisation resulting in strong motivation and better performance.

(4) Enhanced employee growth: Attention to ethics in the workplace helps employees face the reality - both good and bad in the organisation and gain the confidence of dealing with complex work situations.

(5) Ethical programmes help guarantee that personnel policies are legal: A major objective of personnel policies is to ensure ethical treatment of employees. In matters of hiring, evaluating, disciplining, firing etc. An employer can be sued for breach of contract for failure to comply with any promise. The gap between corporate culture and actual practice has significant legal and ethical implications. Attention to ethics ensures highly ethical policies and procedures in the work place. Ethics management programmes are useful in managing diversity. Such programmes require the recognition and application of diverse values and perspectives which are the basis of a sound ethics management programme. Most organisations feel that cost of mechanisms to ensure ethical programme may be more helpful in minimizing the costs of litigations.

(6) Ethical programmes help to detect ethical issues and violations early, so that criminal acts “of omission” may be avoided.

(7) Ethical values help to manage values associated with quality management, strategic planning and diversity management.

17. The concept of Corporate Social Responsibility (CSR) focuses on the idea that beyond making profit, a business has social obligations. It is the responsibility of the companies to produce an overall positive impact on the society. CSR is pursued by business to balance their economic, environmental and social objectives while at the same time addressing stakeholders' expectations and enhancing shareholders' values. Stakeholders, including shareholders, analysts, regulators, labour unions, employees, community organisations and mass media expect companies to be accountable not only for their own performance but for the performance of their entire supply chain. Issues such as peace, sustainable development, security, poverty alleviation, environmental quality and human rights have a profound effect on business and its environment.

Corporate Social Responsibility is the continuing commitment by businesses to behave ethically and contribute to economic development while improving the quality of life of the workforce and their families as well as of the local community and society at large.

Need for social responsibility:

1. The iron law of responsibility
2. To fulfil long term self-interest
3. To establish a better public image
4. To avoid government regulation and control
5. To avoid misuse of National Resources and Economic Power
6. To convert Resistances into Resources
7. To minimise Environmental damage.

18. The root meaning of the term discriminate is "to distinguish one object from another". Employment discrimination is treating one person better than another because of their age, gender, race, religion or other protected class of status. Discrimination in employment is wrong because it violates the basic principle of equality. Discrimination is to treat 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.

Elements of Discrimination: Generally, the discrimination 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 elements which create discrimination 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.

Discrimination in employment is wrong because it violates the basic principle of justice by differentiating between people on the basis of characteristics (race or sex) that are not relevant to the tasks they must perform. Looking to these aspects law has also been changed to conform to these moral requirements and to minimize the discrimination in employment in this respect.

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

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

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

(ii) The objectives of the Central Consumer Protection Council in India are to promote and protect the rights of the consumers such as:-

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

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

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

(d) the right to be heard and to be assured that consumers interest will receive due consideration at appropriate terms;

(e) the right to seek redressal against unfair trade practices;

(f) the right to consumer education.

20. Principles of Ethics: The fundamental principles relating to ethics as applicable to accounting and finance professionals are as follows:

(i) *The principle of integrity*: Integrity means veracity. The principle requires all accounting and finance personnel to be honest and straight-forward in discharging their respective professional duties.

(ii) *The principle of objectivity*: The principle requires accounting and financial professionals to stick to their professional and financial judgement without bias, conflicting interests, or under influence of others.

(iii) *The principle of confidentiality*: The principle requires accounting and financial professionals to refrain from disclosing confidential information related to their work.

(iv) *The principle of professional competence and due care*: The financial and accounting professional need to update their professional skill in the modern competitive environment.

(v) *The principle of professional behavior*: The principle requires accounting and financial professional to comply with relevant laws and regulations and avoid such action which may result into discrediting the profession.

21. The grapevine becomes active when the following factors are present:

(a) Feeling of uncertainty or lack of sense of direction when the organisation is passing through a difficult period.

(b) Feeling of inadequacy or lack of self confidence on the part of the employee, leading to the formation of groups.

(c) Formation of a coterie or favoured group by the manager, giving other employees a feeling of insecurity or isolation. People operating in such circumstances will be filled with all sorts of ideas and will share them with like minded companions, at whatever level they may be. Mostly they find them at their own level, but other levels are not barred. This type of communication is being seriously studied by psychologists and management experts.

22. 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 opinion s

(vi) Willing to listen to the ideas of others.

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

23. Generally, people resist change in an organization. Even after there are some people who accept or welcome change due to the following reasons:

1. **Personal Gain:** People will be more likely to accept change when they see the possibility that they will gain in some of the following areas:-
   - Increased security
   - Money
   - More authority
   - Status/Prestige
   - Better Working Conditions
   - Self-Satisfaction
   - Better Personal Contracts
   - Less time and efforts
2. **Other factors:**
   - Provide a new challenge
   - Respects/like the source
   - Likes the way change is being communicated
   - Reduces boredom
   - Provides opportunity for input
   - Improve future
   - Perception, that the change is necessary.

24. Indemnity Bond

Mr. Somnath S/o ………………….. R/o ………………… do hereby agree to indemnify the Cute Fabrics Ltd. for any loss that may occur for seeking release of dividend for 170 shares of ₹ 1700.

I further declare that personally I have not received the dividend warrant in question.

Mr. Somnath

Date: Signature

Place:

25.

Notice of the First Meeting of the Board of Directors

Ashoka Paper Limited

To, Date

(Director)

Dear Sir/Madam,

This is to inform you that the first meeting of the Board of Directors will be held at the Registered Office of the company on 15th September, 2015 at 3 p.m. to transact the business as per the enclosed agenda.

You are requested to please attend the meeting.

Yours faithfully,

Secretary

For and on behalf of the

Board of Directors

Place : …..

Date ……

Agenda:

(i) Election of the Chairman of the Meeting.

(ii) To produce the Certificate of Incorporation, the Memorandum and the Articles of Association.

(iii) Election of the Chairman of the Company.

(iv) Appointment of Managing Director.

(v) Appointment of Secretary.

(vi) Appointment of Auditors.

(vii) Appointment of Bankers and approval of the opening of a Bank Account and its operation.

(viii) Adoption of the company's seal.

(ix) Approval of the statement of preliminary expenses by the promoters and adoption of the preliminary contracts and underwriting contracts.

(x) Any other business with the permission of the chairman.

PAPER – 3: COST ACCOUNTING AND FINANCIAL MANAGEMENT

PART I: COST ACCOUNTING

QUESTIONS

Material

1. JP Limited, manufacturers of a special product, follows the policy of EOQ (Economic Order Quantity) for one of its components. The component's details are as follows:

	(₹)
Purchase Price Per Component	200
Cost of an Order	100
Annual Cost of Carrying one Unit in Inventory	10% of Purchase Price
Total Cost of Inventory and Ordering Per Annum	4,000

The company has been offered a discount of 2% on the price of the component provided the lot size is 2,000 components at a time.

You are required to:

(a) Compute the EOQ

(b) Advise whether the quantity discount offer can be accepted.

(c) Would your advice differ if the company is offered 5% discount on a single order?

(Assume that the inventory carrying cost does not vary according to discount policy)

Labour

2. Jyoti Ltd. wants to ascertain the profit lost during the year 2014-15 due to increased labour turnover. For this purpose, they have given you the following information:

(1) Training period of the new recruits is 50,000 hours. During this period their productivity is 60% of the experienced workers. Time required by an experienced worker is 10 hours per unit.

(2) 20% of the output during training period was defective. Cost of rectification of a defective unit was ₹ 25.

(3) Potential productive hours lost due to delay in recruitment were 1,00,000 hours.

(4) Selling price per unit is ₹ 180 and P/V ratio is 20%.

(5) Settlement cost of the workers leaving the organization was ₹ 1,83,480.

(6) Recruitment cost was ₹ 1,56,340

(7) Training cost was ₹ 1,13,180

You are required to calculate the profit lost by the company due to increased labour turnover during the year 2014-15.

Overheads

3. In an engineering company, the factory overheads are recovered on a fixed percentage basis on direct wages and the administration overheads are absorbed on a fixed percentage basis on factory cost.

   The company has furnished the following data relating to two jobs undertaken by it in a period:

	Job 101 (₹)	Job 102 (₹)
Direct Materials	54,000	37,500
Direct Wages	42,000	30,000
Selling Price	1,66,650	1,28,250
Profit Percentage on total cost	10%	20%

   Required:

   (i) Computation of percentage recovery rates of factory overheads and administrative overheads.

   (ii) Calculation of the amount of factory overheads, administrative overheads and profit for each of the two jobs.

   (iii) Using the above recovery rates, fix the selling price of job 103. The additional data being.

Direct Materials	₹ 24,000
Direct Wages	₹ 20,000
Profit Percentage on Selling Price	12-1/2%

Non- Integrated Accounts

4. A manufacturing company disclosed a net loss of ₹ 3,47,000 as per their Cost Accounts for the year ended March 31, 2016. The Financial Accounts however disclosed a net loss of ₹ 5,10,000 for the same period. The following information was revealed as a result of scrutiny of the figures of both the sets of accounts.

	(₹)
(i) Factory Overheads under-absorbed	40,000
(ii) Administration Overheads over-absorbed	60,000
(iii) Depreciation charged in Financial Accounts	3,25,000
(iv) Depreciation charged in Cost Accounts	2,75,000

(v) Interest on investments not included in Cost Accounts	96,000
(vi) Income-tax provided	54,000
(vii) Interest on loan funds in Financial Accounts	2,45,000
(viii) Transfer fees (credit in financial books)	24,000
(ix) Stores adjustment (credit in financial books)	14,000
(x) Dividend received	32,000

Prepare a memorandum Reconciliation Account.

Operating Costing

5. JRP Resorts (P) Ltd. offers three types of rooms to its guests, viz Deluxe room, Super Deluxe room and Luxury Suite. You are required to ascertain the tariff to be charged to the customers for different types of rooms on the basis of following information:

Type of Room	Number of Rooms	Occupancy
Deluxe Room	100	90%
Super Deluxe Room	60	75%
Luxury Suite	40	60%

Rent of 'Super Deluxe' room is to be fixed at 2 times of 'Deluxe room' and that of 'Luxury Suite' is 3 times of 'Deluxe room'. Annual expenses are as follows:

Particulars	Amount (₹in lakhs)
Staff salaries	680.00
Lighting, Heating and Power	300.00
Repairs, Maintenance and Renovation	180.00
Linen	30.00
Laundry charges	24.00
Interior decoration	75.00
Sundries	30.28

An attendant for each room was provided when the room was occupied and he was paid ₹ 500 per day towards wages. Further, depreciation is to be provided on building @ 5% on ₹ 900 lakhs, furniture and fixtures @ 10% on ₹ 90 lakhs and air conditioners @ 10% on ₹ 75 lakhs.

Profit is to be provided @ 25% on total taking and assume 360 days in a year.

Process Costing

6. From the following Information for the month ending October, 2015, prepare Process Cost accounts for Process III. Use First-in-fist-out (FIFO) method to value equivalent production.

Direct materials added in Process III (Opening WIP)	2,000 units at ₹ 25,750
Transfer from Process II	53,000 units at ₹ 4,11,500
Transferred to Process IV	48,000 units
Closing stock of Process III	5,000 units
Units scrapped	2,000 units
Direct material added in Process III	₹ 1,97,600
Direct wages	₹ 97,600
Production Overheads	₹ 48,800

Degree of completion:

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

The normal loss in the process was 5% of production and scrap was sold at ₹ 3 per unit.

Joint Products and By Products

7. A company processes a raw material in its Department 1 to produce three products, viz. A, B and X at the same split-off stage. During a period 1,80,000 kgs of raw materials were processed in Department 1 at a total cost of ₹ 12,88,000 and the resultant output of A, B and X were 18,000 kgs, 10,000 kgs and 54,000 kgs respectively. A and B were further processed in Department 2 at a cost of ₹ 1,80,000 and ₹ 1,50,000 respectively.

   X was further processed in Department 3 at a cost of ₹1,08,000. There is no waste in further processing. The details of sales affected during the period were as under:

	A	B	X
Quantity Sold (kgs.)	17,000	5,000	44,000
Sales Value (₹)	12,24,000	2,50,000	7,92,000

   There were no opening stocks. If these products were sold at split-off stage, the selling prices of A, B and X would have been ₹ 50, ₹ 40 and ₹ 10 per kg respectively. Required:

   (i) Prepare a statement showing the apportionment of joint costs to A, B and X.

(ii) Present a statement showing the cost per kg of each product indicating joint cost and further processing cost and total cost separately.

(iii) Prepare a statement showing the product wise and total profit for the period.

(iv) State with supporting calculations as to whether any or all the products should be further processed or not

Contract Costing

8. A contractor commenced a building contract on October 1, 2013. The contract price is ₹ 4,40,000. The following data pertaining to the contract for the year 2014-15 has been compiled from his books and is as under:

		(₹)
April, 2014	Work-in-progress not certified	55,000
	Materials at site	2,000
2014-15	Expenses incurred:	
	Materials issued	1,12,000
	Wages paid	1,08,000
	Hire of plant	20,000
	Other expenses	34,000
March 31, 2015	Materials at site	4,000
	Work-in-progress: Not certified	8,000
	Work-in-progress: Certified	4,05,000

The cash received represents 80% of work certified. It has been estimated that further costs to complete the contract will be ₹23,000 including the materials at site as on March 31, 2015.

Required

Determine the profit on the contract for the year 2014-15 on prudent basis, which has to be credited to Costing P/L A/c.

Standard Costing

9. The following information has been provided by a company:

Number of units produced and sold	6,000
Standard labour rate per hour	₹ 8
Standard hours required for 6,000 units	-
Actual hours required	17,094 hours

Labour efficiency 105.3%

Labour rate variance ₹ 68,376 (A)

You are required to calculate:

(i) Actual labour rate per hour

(ii) Standard hours required for 6,000 units

(iii) Labour Efficiency variance

(iv) Standard labour cost per unit

(v) Actual labour cost per unit.

Marginal Costing

10. You are given the following data for the year 2015 of Rio Co. Ltd:

Variable cost	60,000	60%
Fixed cost	30,000	30%
Net profit	10,000	10%
Sales	1,00,000	100%

Find out (a) Break-even point, (b) P/V ratio, and (c) Margin of safety. Also draw a break-even chart showing contribution and profit.

SUGGESTED HINTS/ANSWERS

1. (a) Computation of EOQ

(i) Purchase price per component (C_1) ₹ 200

(ii) Cost of an order (C_0) ₹ 100

(iii) Annual cost of carrying one unit of inventory is ($i \times C_1$) 10% of C_1 or ₹ 20

(iv) Total cost of carrying inventory and ordering per annum ₹ 4,000

(v) Let the total annual inventory usage be S.

To compute E.O.Q. by using the above data we require the figure of total annual usage of inventory. This can be determined by making use of the following relation.

$$\sqrt{2SC_0iC_1} = ₹\ 4{,}000$$

$$\text{Or, } \sqrt{2S \times ₹100 \times ₹20} = ₹\ 4{,}000$$

Or, $\sqrt{4{,}000\text{S}}$ = ₹ 4,000

Squaring both side

Or, 4,000S = 4,000 × 4,000 Or, S = 4,000 units

Now

$$\text{E.O.Q.} = \sqrt{\frac{2SC_0}{iC_1}} = \sqrt{\frac{2 \times 4{,}000 \times ₹100}{₹20}} = 200 \text{ units}$$

Alternatively, EOQ can also be calculated as below:

Lets EOQ is 'Q', then average holding inventories are $\frac{Q}{2}$ and annual carrying cost is $\frac{Q}{2} \times ₹20 = 10Q$

Now at EOQ level carrying cost and ordering cost is equal i.e. ₹ 2,000 each.

So, 10Q = ₹ 2,000 and Q = $\frac{₹2{,}000}{10} = 200$

Hence, EOQ = 200 units

Note: Different logical notations can be used to express variables in the formula.

(b) When order size is 2,000 units

No. of orders = $\frac{4{,}000 \text{ units}}{2{,}000 \text{ units}} = 2$

Total cost = Ordering Cost + Carrying Cost

= 2× ₹ 100 + 1/2 × 2,000 units × ₹ 20

= ₹ 200 + ₹ 20,000 = ₹ 20,200

∴ Extra cost = ₹ 20,200 – ₹ 4,000 = ₹ 16,200

Quantity discount received = 2% × 4,000 units × ₹ 200

= ₹ 16,000

Advice to Management: The quantity discount offer should not be accepted as it results in additional expenditure of ₹ 200 (₹ 16,200 – ₹ 16,000)

(c) When order size is 4,000 units

No. of orders = $\frac{4{,}000 \text{ units}}{4{,}000 \text{ units}} = 1$

Total cost = 1 × ₹ 100 + 1/2 × 4,000 units × ₹ 20 = ₹ 40,100

∴ Extra cost = ₹ 40,100 – ₹ 4,000 = ₹ 36,100

Quantity discount received = 5% × 4,000 units × ₹ 200

= ₹ 40,000

Advice to Management: The quantity discount offer should be accepted as it result in reducing the total cost of carrying and ordering of inventory to the extent of ₹ 3,900 [₹ 40,000 – ₹ 36,100].

Note: White solving this problem, total cost of inventory and ordering cost per annum, has been considered as total cost of carrying inventory and ordering per annum.

2. Output by experienced workers in 50,000 hours = $\frac{50,000}{10}$ = 5,000 units

∴ Output by new recruits = 60% of 5,000 = 3,000 units

Loss of output = 5,000 – 3,000 = 2,000 units

Total loss of output = Due to delay recruitment + Due to inexperience

= 10,000 + 2,000 = 12,000 units

Contribution per unit = 20% of ₹180 = ₹ 36

Total contribution lost = ₹36 × 12,000 units = ₹ 4,32,000

Cost of repairing defective units = 3,000 units × 0.2 × ₹ 25 = ₹ 15,000

Profit forgone due to labour turnover

	(₹)
Loss of Contribution	4,32,000
Cost of repairing defective units	15,000
Recruitment cost	1,56,340
Training cost	1,13,180
Settlement cost of workers leaving	1,83,480
Profit forgone in 2014-15	9,00,000

3. **(i)** Let factory overhead recovery rate, as percentage of direct wages be F and administrative overheads recovery rate, as percentage of factory cost be A.

Factory Cost of Jobs:

Job 101 = ₹ 96,000 + ₹ 42,000F

Job 102 = ₹ 67,500 + ₹ 30,000F

Total Cost of Production of Jobs:

Job 101 = (₹ 96,000 + ₹ 42,000F) + (₹ 96,000 + ₹ 42,000 F) A= ₹ 1,51,500………(i)

Job 102 = (₹ 67,500 + ₹ 30,000F) + (₹ 67,500 + ₹ 30,000 F) A = ₹ 1,06,875……..(ii)

(Refer to Working Note)

42,000 F + 96,000 A + 42,000 FA = 55,500……………………………………….(iii) × 5

30,000 F + 67,500 A + 30,000 FA = 39,375………………………..…………..(iv) × 7

On solving above relations

$$\begin{array}{ll} \cancel{2,10,000\ F} + 4,80,000\ A + \cancel{2,10,000\ FA} & = 2,77,500 \\ \underline{\cancel{2,10,000\ F} + 4,72,500\ A + \cancel{2,10,000\ FA}} & \underline{= 2,75,625} \\ \qquad 7,500\ A & = 1,875 \\ \qquad\qquad A & = 0.25 \end{array}$$

Putting the value of ‘A’ in equation no. (iv) above to get the value of ‘F’

30,000 F + 67,500 × 0.25 + 30,000 × 0.25 F = 39,375

37,500 F = 39,375 – 16,875 or, F = 0.60

Hence percentage recovery rates of factory overheads and administrative overheads are 60% and 25% respectively.

Working Note:

	Job 101	Job 102
Total cost of production (₹) $\frac{\text{Selling price}}{(100\% + \text{Percentage of profit})}$	1,51,500 (₹ 1,66,650/110%)	1,06,875 (₹ 1,28,250/120%)

(ii) Statement of jobs, showing amount of factory overheads, administrative overheads and profit

	Job 101 (₹)	Job 102 (₹)
Direct Materials	54,000	37,500
Direct Wages	42,000	30,000
Prime Cost	96,000	67,500
Factory Overheads (60% of Direct Wages*)	25,200	18,000
Factory Cost	1,21,200	85,500
Administrative Overheads (25% of Factory Cost*)	30,300	21,375
Total Cost	1,51,500	1,06,857
Profit (difference figure)	15,150	21,375
Selling Price	1,66,650	1,28,250

* As calculated in requirement (i) above.

(iii) Selling price of Job 103

	(₹)
Direct Materials	24,000
Direct Wages	20,000
Prime Cost	44,000
Factory overheads (60% of Direct Wages*)	12,000
Factory Cost	56,000
Administrative Overheads (25% of Factory Cost*)	14,000
Total Cost	70,000
Profit Margin (difference figure)	10,000
Selling Price $\left[\frac{\text{Total cost}}{87.5\%}\right]$	80,000

* As calculated in requirement (i) above.

4. Memorandum Reconciliation Account

Dr. **Cr.**

	(₹)		(₹)
To Net Loss as per Costing books	3,47,000	By Administration overheads over recovered in cost accounts	60,000
To Factory overheads under absorbed in Cost Accounts	40,000	By Interest on investment not included in Cost Accounts	96,000
To Depreciation under charged in Cost Accounts	50,000	By Transfer fees in Financial books	24,000
To Income-Tax not provided in Cost Accounts	54,000	By Stores adjustment (Credit in financial books)	14,000
To Interest on Loan Funds in Financial Accounts	2,45,000	By Dividend received in financial books	32,000
		By Net loss as per Financial books	5,10,000
	7,36,000		7,36,000

5. Operating cost statement of JRP Resort (P) Limited

Particulars	Cost per annum (₹ in lakhs)
Staff Salaries	680.00
Lighting, Heating & Power	300.00

Repairs, Maintenance & Renovation	180.00
Linen	30.00
Laundry charges	24.00
Interior Decoration	75.00
Sundries	30.28
Room Attendant's Wages (Working Note 3)	286.20
Depreciation (Working Note 4)	61.50
Total cost for the year	1666.98

Computation of profit:

Let ₹ x be the rent for Deluxe room.

Equivalent deluxe room days are 90,720 (Working Note 2)

Total takings = ₹ 90,720x

Profit is 25% of total takings.

Profit = 25% of ₹ 90,720x = ₹ 22,680x

Total takings = Total Cost + Profit

₹ 90,720x = ₹ 16,66,98,000 + ₹ 22,680x

₹ 90,720x - ₹ 22,680x = ₹ 16,66,98,000

₹ 68,040x = ₹ 16,66,98,000

$$X = \frac{₹\ 16,66,98,000}{₹\ 68,040} = ₹\ 2,450$$

Rent to be charged for Deluxe room	₹ 2,450
Rent to be charged for Super Deluxe room (₹ 2,450 × 2)	₹ 4,900
Rent to be charged for Luxury Suite (₹ 2,450 × 3)	₹ 7,350

Working Notes:

1. **Computation of Room Occupancy**

Type of Room	No. of rooms × No. of days × Occupancy %	Room days
Deluxe Room	100 rooms × 360 days × 90% occupancy	32,400
Super Deluxe Room	60 rooms × 360 days × 75% occupancy	16,200
Luxury Suite	40 rooms × 360 days × 60% occupancy	8,640
	Total	57,240

2. Computation of equivalent Deluxe room days

Rent of 'Super Deluxe' room is to be fixed at 2 times of 'Deluxe room' and Luxury Suite' is 3 times of 'Deluxe room'. Therefore equivalent room days would be:

Type of Room	Room days	Equivalent Deluxe room days
Deluxe Room	32,400 × 1	32,400
Super Deluxe Room	16,200 × 2	32,400
Luxury Suite	8,640 × 3	25,920
	Total	90,720

3. Computation of room attendant's wages

Room occupancy days × ₹ 500 per day

57,240 room-days × ₹500 = ₹ 2,86,20,000

4. Computation of Depreciation per annum

Particulars	Cost (₹)	Rate of Depreciation	Depreciation (₹)
Building	900,00,000	5%	45,00,000
Furniture & Fixtures	90,00,000	10%	9,00,000
Air Conditioners	75,00,000	10%	7,50,000
			61,50,000

6. Statement of Equivalent Production

Input		Output		Equivalent production					
Item	Units	Item	Units	Material A		Material B		Lab.& OHs.	
				Units	%	Units	%	Units	%
Op stock	2,000	Work on op WIP	2,000	-	-	400	20	800	40
Process II transfer	53,000	Introduced & completed during the period (48,000 – 2000)	46,000	46,000	100	46,000	100	46,000	100
			48,000						
		Normal Loss (2,000,+,53,000 – 5,000) x 5%	2,500	-	-	-	-	-	-

		Closing WIP	5,000	5,000	100	3,500	70	2,500	50
			55,500	51,000		49,900		49,300	
		Abnormal Gain	500	500	100	500	100	500	100
	55,000		55,000	50,500		49,400		48,800	

*Material A represents transfer-in units from Process-II

Statement of Cost for each Element

Element of cost	Cost (₹)	Equivalent Production	Cost per unit (₹)
Material A			
- Transferred from Process-II	4,11,500		
- Less: Scrap realisation (2,500 × ₹ 3)	(7,500)		
	4,04,000	50,500	8.00
Material B	1,97,600	49,400	4.00
Wages	97,600	48,800	2.00
Overheads	48,800	48,800	1.00
	7,48,000		15.00

Process Cost Sheet (in ₹)

Opening W-I-P:	
- Material B (400 × ₹ 4)	1,600
- Wages (800 × ₹ 2)	1,600
- Overheads (800 × ₹1)	800
	4,000
Introduced and completely processed during the period (46,000 × ₹ 15)	6,90,000
Closing W-I-P:	
Material A (5,000 × ₹ 8)	40,000
Material B (3,500 × ₹ 4)	14,000
Wages (2,500 × ₹ 2)	5,000
Overheads (2,500 × ₹ 1)	2,500
	61,500
Abnormal Gain (500 × ₹ 15)	7,500

Process III A/c

	Units	Amount		Units	Amount
To Balance b/d	2,000	25,750	By Normal Loss	2,500	7,500
To Process II A/c	53,000	4,11,500	By Process IV A/c (6,90,000 + 4,000+ 25,750)	48,000	7,19,750
To Direct Material		1,97,600	By Bal c/d	5,000	61,500
To Direct Wages		97,600			
To Prodn OHs		48,800			
To Abnormal Gain	500	7,500			
	55,500	7,88,750		55,500	7,88,750

7. (i) **Statement showing the apportionment of joint costs to A, B and X**

Products	A	B	X	Total
Output (kg)	18,000	10,000	54,000	
Sales value at the point of split off (₹)	9,00,000 (₹ 50 x 18,000)	4,00,000 (₹ 40 x 10,000)	5,40,000 (₹ 10 x 54,000)	18,40,000
Joint cost apportionment on the basis of sales value at the point of split off (₹)	6,30,000 $\left(\frac{₹\,12,88,000}{₹\,18,40,000} \times ₹\,9,00,000\right)$	2,80,000 $\left(\frac{₹\,12,88,000}{₹\,18,40,000} \times ₹\,4,00,000\right)$	3,78,000 $\left(\frac{₹\,12,88,000}{₹\,18,40,000} \times ₹\,5,40,000\right)$	12,88,000

(ii) **Statement showing the cost per kg. of each product (indicating joint cost; further processing cost and total cost separately)**

Products	A	B	X
Joint costs apportioned (₹) : (I)	6,30,000	2,80,000	3,78,000
Production (kg) : (II)	18,000	10,000	54,000
Joint cost per kg (₹): (I ÷ II)	35	28	7
Further processing Cost per kg. (₹)	10 $\left(\frac{₹\,1,80,000}{18,000\,\text{kg}}\right)$	15 $\left(\frac{₹\,1,50,000}{10,000\,\text{kg}}\right)$	2 $\left(\frac{₹\,1,08,000}{54,000\,\text{kg}}\right)$
Total cost per kg (₹)	45	43	9

(iii) Statement showing the product wise and total profit for the period

Products	A	B	X	Total
Sales value (₹)	12,24,000	2,50,000	7,92,000	
Add: Closing stock value (₹) (Refer to Working note 2)	45,000	2,15,000	90,000	
Value of production (₹)	12,69,000	4,65,000	8,82,000	26,16,000
Apportionment of joint cost (₹)	6,30,000	2,80,000	3,78,000	
Add: Further processing cost (₹)	1,80,000	1,50,000	1,08,000	
Total cost (₹)	8,10,000	4,30,000	4,86,000	17,26,000
Profit (₹)	4,59,000	35,000	3,96,000	8,90,000

Working Notes

1.

Products	A	B	X
Sales value (₹)	12,24,000	2,50,000	7,92,000
Quantity sold (Kgs.)	17,000	5,000	44,000
Selling price ₹/kg	72 $\left(\frac{₹\,12,24,000}{17,000\,kg}\right)$	50 $\left(\frac{₹\,2,50,000}{5,000\,kg}\right)$	18 $\left(\frac{₹\,7,92,000}{44,000\,kg}\right)$

2. Valuation of closing stock:

Since the selling price per kg of products A, B and X is more than their total costs, therefore closing stock will be valued at cost.

Products	A	B	X	Total
Closing stock (kgs.)	1,000	5,000	10,000	
Cost per kg (₹)	45	43	9	
Closing stock value (₹)	45,000 (₹ 45 x 1,000 kg)	2,15,000 (₹ 43 x 5,000 kg)	90,000 (₹9x10,000 kg)	3,50,000

(iv) Calculations for processing decision

Products	A	B	X
Selling price per kg at the point of split off (₹)	50	40	10
Selling price per kg after further processing (₹) (Refer to working Note 1)	72	50	18

Incremental selling price per kg (₹)	22	10	8
Less: Further processing cost per kg (₹)	(10)	(15)	(2)
Incremental profit (loss) per kg (₹)	12	(5)	6

Product A and X has an incremental profit per unit after further processing, hence, these two products may be further processed. However, further processing of product B is not profitable hence, product B shall be sold at split off point.

8. **Contract Account**
For the year 2014-15

Dr. Cr.

Particulars	**(₹)**	**Particulars**	**(₹)**
01.04.14 To Work in-progress (not certified)	55,000	By Materials at site	4,000
To Materials at site	2,000		
2014-15 To Materials issued To Wages paid To Hire of plant To Other expenses	 1,12,000 1,08,000 20,000 34,000	 By Cost of contract c/d (to date)	 3,27,000
	3,31,000		3,31,000
31.03.15 To Cost of contract b/d (to date)	3,27,000	By Work-certified	4,05,000
To Costing Profit & Loss A/c	66,273	By Work-not certified	8,000
To Profit in reserve	19,727		
	4,13,000		4,13,000

Profit for the year 2014-15

= ₹ 4,13,000 – ₹ 3,27,000 = ₹ 86,000

Estimated profit (on the completion of the contract)

	(₹)
Cost of the contract (to date)	3,27,000
Further cost of completing the contract	23,000
Total cost : (A)	3,50,000
Contract price: (B)	4,40,000

Estimated profit on the completion of contract: [(A)–(B)] ₹ 90,000

Since $\left(\frac{\text{Work certified}}{\text{Contract price}}\right) \times 100 = \frac{₹\ 4,05,000}{₹\ 4,40,000} \times 100 = 92.05\%$

This implies that contract is nearing completion. Hence the profit to be taken to Costing Profit and Loss Account on prudent basis will be given by the formula:

$= \text{Estimated profit} \times \frac{\text{Work certified}}{\text{Contract price}} \times \frac{\text{Cash received}}{\text{Work certified}}$

$= ₹\ 90,000 \times \frac{₹\ 4,05,000}{₹\ 4,40,000} \times \frac{₹\ 3,24,000}{₹\ 4,05,000}$

$=$ ₹ 66,273

9. SR – Standard labour Rate per Hour

AR – Actual labour rate per hour

SH – Standard Hours

AH – Actual hours

(i) Actual labour rate per hour:

Labour rate Variance = AH (SR – AR)

= 17,094 (₹8 – AR) = 68,376 (A) = - 68,376

= ₹ 8 – AR = - 4

Or, AR = ₹ 12

(ii) Standard hour required for 6,000 units:

Labour Efficiency $= \frac{SH}{AH} \times 100 = 105.3$

$= SH = \frac{AH \times 105.3}{100} = \frac{17,094 \text{ hours} \times 105.3}{100}$

= 17,999.982 or, SH = 18,000 hours

(iii) Labour Efficiency Variance = SR (SH – AH)

= ₹ 8(18,000 – 17,094)

= 8 × 906 = ₹ 7,248 (F)

(iv) Standard Labour Cost per Unit $= \frac{18,000 \text{ hours} \times ₹\ 8}{6,000 \text{ units}} = ₹\ 24$

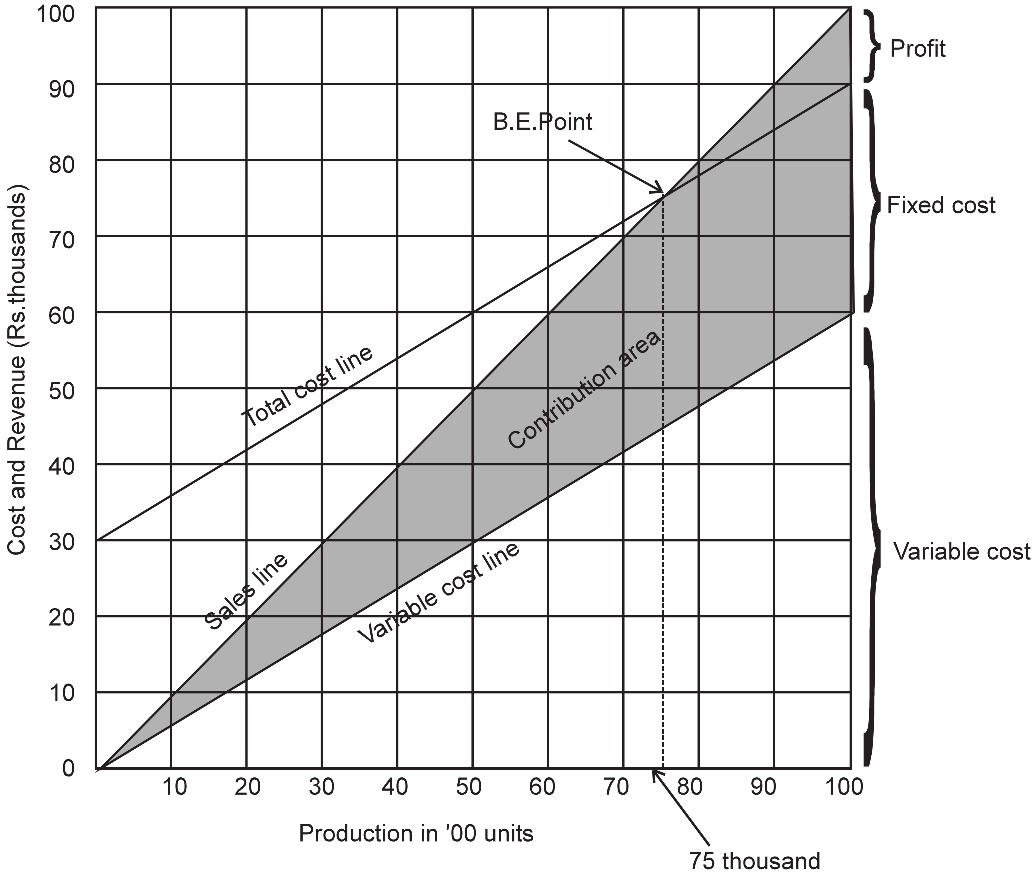
(v) Actual Labour Cost per Unit $= \dfrac{17{,}094 \text{ hours} \times ₹\ 12}{6{,}000 \text{ units}} = ₹\ 34.19$

10. P/V Ratio $= \dfrac{S - V}{S} = \dfrac{₹1{,}00{,}000 - ₹\ 60{,}000}{₹1{,}00{,}000} \times 100 = 40\%$

BE point $= \dfrac{F}{\text{P/V ratio}} = \dfrac{30{,}000}{40\%} = ₹\ 75{,}000$

Margin of safety = Actual Sales – BE point= 1,00,000 – 75,000 = ₹ 25,000

Break even chart showing contribution is shown below:



Break-even chart

PART II: FINANCIAL MANAGEMENT

QUESTIONS

Time Value of Money

1. Calculate if ₹10,000 is invested at interest rate of 12% per annum, what is the amount after 3 years if the compounding of interest is done?

   (i) Annually

   (ii) Semi-annually

   (iii) Quarterly

Fund Flow Statement

2. ABC Ltd. has supplied the following information at the beginning and at the end of the year 2015-16:

	1.4.2015	31.3.2016
	(₹)	(₹)
Plant less depreciation	95,000	2,13,000
Investment (long term)	1,98,000	4,35,000
Debentures	3,75,000	1,05,000
Equity share capital	6,00,000	6,00,000
Reserves & Surplus	3,57,000	6,15,000

Although ABC Ltd. could not provide complete Balance Sheet and Profit & Loss Account, it supplied the following further information:

(1) An interim dividend of ₹ 54,000 has been paid during the year 2015-16.

(2) The net income includes ₹ 20,000 on account of profit on sale of plant. There has been an increase of ₹ 1,40,000 in the gross value of plant after a plant having gross value of ₹ 43,500, whose written down value was ₹ 28,500, was disposed off during the year.

From the information given above, you are required to prepare a Funds Flow Statement.

Ratio Analysis

3. The following are the accounting information and financial ratios of PQR Ltd. related to the year ended 31st December, 2015:

		2015
I	Accounting Information:	
	Gross Profit	15% of Sales
	Net profit	8% of sales
	Raw materials consumed	20% of works cost
	Direct wages	10% of works cost
	Stock of raw materials	3 months' usage
	Stock of finished goods	6% of works cost
	Debt collection period	60 days
	All sales are on credit	
II	Financial Ratios:	
	Fixed assets to sales	1 : 3
	Fixed assets to Current assets	13 : 11
	Current ratio	2 : 1
	Long-term loans to Current liabilities	2 : 1
	Capital to Reserves and Surplus	1 : 4

If value of fixed assets as on 31st December, 2014 amounted to ₹ 26 lakh, prepare a summarised Profit and Loss Account of the company for the year ended 31st December, 2015 and also the Balance Sheet as on 31st December, 2015.

Cost of Capital

4. As a financial analyst of a large electronics company, you are required to determine the weighted average cost of capital of the company using (a) book value weights and (b) market value weights. The following information is available for your perusal.

The Company's present book value capital structure is:

	(₹)
Debentures (₹ 100 per debenture)	8,00,000
Preference shares (₹ 100 per share)	2,00,000
Equity shares (₹ 10 per share)	10,00,000
	20,00,000

All these securities are traded in the capital markets. Recent prices are:

Debentures, ₹110 per debenture, Preference shares, ₹120 per share, and Equity shares, ₹ 22 per share

Anticipated external financing opportunities are:

(i) ₹ 100 per debenture redeemable at par; 10 year maturity, 11 per cent coupon rate, 4 per cent flotation costs, sale price, ₹ 100

(ii) ₹ 100 preference share redeemable at par; 10 year maturity, 12 per cent dividend rate, 5 per cent flotation costs, sale price, ₹100.

(iii) Equity shares: ₹ 2 per share flotation costs, sale price = ₹ 22.

In addition, the dividend expected on the equity share at the end of the year is ₹ 2 per share, the anticipated growth rate in dividends is 7 per cent and the firm has the practice of paying all its earnings in the form of dividends. The corporate tax rate is 35 per cent.

Capital Structure

5. Akash Limited provides you the following information:

	(₹)
Profit (EBIT)	2,80,000
Less: Interest on Debenture @ 10%	40,000
EBT	2,40,000
Less Income Tax @ 50%	1,20,000
	1,20,000
No. of Equity Shares (₹ 10 each)	30,000
Earnings per share (EPS)	4
Price /EPS (PE) Ratio	10

The company has reserves and surplus of ₹ 7,00,000 and required ₹ 4,00,000 further for modernisation. Return on Capital Employed (ROCE) is constant. Debt (Debt/ Debt + Equity) Ratio higher than 40% will bring the P/E Ratio down to 8 and increase the interest rate on additional debts to 12%. You are required to ascertain the probable price of the share.

(i) If the additional capital are raised as debt; and

(ii) If the amount is raised by issuing equity shares at ruling market price.

Leverage

6. A Company had the following Balance Sheet as on March 31, 2015:

Equity and Liabilities	(₹ in crore)	Assets	(₹ in crore)
Equity Share Capital (10 crore shares of ₹ 10 each)	100	Fixed Assets (Net)	250
Reserves and Surplus	20	Current Assets	150
15% Debentures	200		

Current Liabilities	80		
	400		400

The additional information given is as under:

Fixed Costs per annum (excluding interest)	₹ 80 crores
Variable operating costs ratio	65%
Total Assets turnover ratio	2.5
Income-tax rate	40%

Required:

Calculate the following and comment:

(i) Earnings per share

(ii) Operating Leverage

(iii) Financial Leverage

(iv) Combined Leverage.

Capital Budgeting

7. Navya Limited is thinking of replacing its existing machine by a new machine which would cost ₹ 60 lakhs. The company's current production is 80,000 units, and is expected to increase to 1,00,000 units, if the new machine is bought. The selling price of the product would remain unchanged at ₹ 200 per unit. The following is the cost of producing one unit of product using both the existing and new machine:

(Unit Cost in ₹)

	Existing Machine (80,000 units)	**New Machine (1,00,000 units)**	**Difference**
Materials	75.00	63.75	(11.25)
Wages & Salaries	51.25	37.50	(13.75)
Supervision	20.00	25.00	5.00
Repairs and Maintenance	11.25	7.50	(3.75)
Power and Fuel	15.50	14.25	(1.25)
Depreciation	0.25	5.00	4.75
Allocated Corporate Overheads	10.00	12.50	2.50
	183.25	165.50	(17.75)

The existing machine has an accounting book value of ₹ 1,00,000, and it has been fully depreciated for tax purpose. It is estimated that machine will be useful for 5 years. The supplier of the new machine has offered to accept the old machine for ₹ 2,50,000. However, the market price of old machine today is ₹ 1,50,000 and it is expected to be ₹

35,000 after 5 years. The new machine has a life of 5 years and a salvage value of ₹ 2,50,000 at the end of its economic life. Assume corporate Income tax rate at 40%, and depreciation is charged on straight line basis for Income-tax purposes. Further assume that book profit is treated as ordinary income for tax purpose. The opportunity cost of capital of the Company is 15%.

Required:

(i) Estimate net present value of the replacement decision.

(ii) Estimate the internal rate of return of the replacement decision.

(iii) Should Company go ahead with the replacement decision? Suggest.

Year (t)	1	2	3	4	5
$PVIF_{0.15,t}$	0.8696	0.7561	0.6575	0.5718	0.4972
$PVIF_{0.20,t}$	0.8333	0.6944	0.5787	0.4823	0.4019
$PVIF_{0.25,t}$	0.8000	0.6400	0.5120	0.4096	0.3277
$PVIF_{0.30,t}$	0.7692	0.5917	0.4552	0.3501	0.2693
$PVIF_{0.35,t}$	0.7407	0.5487	0.4064	0.3011	0.2230

Working Capital Management

8. A company is considering its working capital investment and financial policies for the next year. Estimated fixed assets and current liabilities for the next year are ₹ 2.60 crores and ₹ 2.34 crores respectively. Estimated Sales and EBIT depend on current assets investment, particularly inventories and book-debts. The Financial Controller of the company is examining the following alternative Working Capital Policies:

(₹ in crore)

Working Capital Policy	Investment in Current Assets	Estimated Sales	EBIT
Conservative	4.50	12.30	1.23
Moderate	3.90	11.50	1.15
Aggressive	2.60	10.00	1.00

After evaluating the working capital policy, the Financial Controller has advised the adoption of the moderate working capital policy. The company is now examining the use of long-term and short-term borrowings for financing its assets. The company will use ₹ 2.50 crores of the equity funds. The corporate tax rate is 35%. The company is considering the following debt alternatives.

(₹ in crore)

Financing Policy	Short-term Debt	Long-term Debt
Conservative	0.54	1.12

Moderate	1.00	0.66
Aggressive	1.50	0.16
Interest rate-Average	12%	16%

You are required to calculate the following:

(i) Working Capital Investment for each policy:

(a) Net Working Capital position

(b) Rate of Return

(c) Current ratio

(ii) Financing for each policy:

(a) Net Working Capital position.

(b) Rate of Return on Shareholders' equity.

(c) Current ratio.

Introduction and type of financing

9. Write short notes on the following:

(a) Functions of Finance Manager.

(b) Inter relationship between investment, financing and dividend decisions.

(c) Debt securitisation

SUGGESTED HINTS/ANSWERS

1. Computation of future value

Principal (P) = ₹ 10,000

Rate of interest (i) = 12% p.a.

Time period (n) = 3 years

Amount if compounding is done:

(i) Annually

Future Value $= P(1+i)^n$

$= ₹\ 10,000\ (1 + 0.12)^{3\times1}$

$= ₹\ 10,000 \times 1.404928$

$= ₹\ 14,049.28$

(ii) Semi Annually

Future Value $= ₹10{,}000 \left(1+\frac{12}{100\times 2}\right)^{3\times 2}$

$= ₹10{,}000\ (1 + 0.06)^{6}$

$= ₹10{,}000 \times 1.418519$

$= ₹\ 14{,}185.19$

(iii) Quarterly

Future Value $= ₹10{,}000 \left(1+\frac{12}{100\times 4}\right)^{3\times 4}$

$= ₹10{,}000\ (1 + 0.03)^{12}$

$= ₹10{,}000 \times 1.425761$

$= ₹\ 14{,}257.61$

2. Fund from Operation

Particulars	**(₹)**
Closing value of reserves & surplus	6,15,000
Less: Opening value of reserves & surplus	(3,57,000)
Profit after depreciation	2,58,000
Add: Depreciation (refer the working note)	37,000
Profit before depreciation	2,95,000
Less: Profit on sale of plant	(20,000)
	2,75,000
Add: Interim dividend	54,000
Fund from Operation	3,29,000

Fund flow statement for the year ended 31st March 2016

Particulars	**(₹)**
Sources of Fund	
Fund from Operation	3,29,000
Decrease in working capital (Balancing Figure)	3,67,000
Sale of plant	48,500
	7,44,500

Application of Fund	
Long-term Investment (₹4,35,000 – ₹1,98,000)	2,37,000
Purchase of Plant (refer the working note)	1,83,500
Repayment of Debentures (₹3,75,000 – ₹1,05,000)	2,70,000
Payment of interim dividend	54,000
	7,44,500

Working Note:

Plant A/c

Particulars	**(₹)**	**Particulars**	**(₹)**
To Balance b/d	95,000	By Bank A/c (Sale)	48,500
To P&L A/c (Profit on sale)	20,000	By Prov. for Depreciation (Balancing figure)	37,000
To Bank A/c (new purchase) (₹1,40,000 + ₹43,500)	1,83,500	By Balance c/d	2,13,000
	2,98,500		2,98,500

3. (a) Working Notes:

(i) Calculation of Sales:

$$\frac{\text{Fixed Assets}}{\text{Sales}} = \frac{1}{3} \quad \text{or,} \quad \frac{₹26,00,000}{\text{Sales}} = \frac{1}{3}$$

Or, Sales = ₹ 78,00,000

(ii) Calculation of Current Assets:

$$\frac{\text{Fixed Assets}}{\text{Current Assets}} = \frac{13}{11} \quad \text{or,} \quad \frac{₹26,00,000}{\text{Current Assets}} = \frac{13}{11}$$

Or, Current Assets = ₹ 22,00,000

(iii) Calculation of Raw Material Consumption and Direct Wages:

	(₹)
Sales	78,00,000
Less: Gross Profit (15% of ₹78,00,000)	11,70,000
Works Cost	66,30,000

Raw Material Consumption (20% of ₹66,30,000) = ₹ 13,26,000

Direct Wages (10% of ₹66,30,000) = ₹ 6,63,000

(iv) Calculation of Stock of Raw Materials (3 months usage):

$$= ₹13,26,000 \times \frac{3\,\text{months}}{12\,\text{months}} = ₹\ 3,31,500$$

(v) Calculation of Stock of Finished Goods (6% of Works Cost):

= 6% of ₹ 66,30,000 = ₹ 3,97,800

(vi) Calculation of Current Liabilities:

$$\frac{\text{Current Assets}}{\text{Current Liablities}} = \frac{2}{1} \text{ or, } \frac{₹22,00,000}{\text{Current Liablities}} = \frac{2}{1}$$

Or, Current Liabilities = ₹ 11,00,000

(vii) Calculation of Debtors:

$$\text{Average collection period} = \frac{\text{Debtors}}{\text{Credit Sales}} \times 365*$$

$$\frac{\text{Debtors}}{₹78,00,000} \times 365 \text{ days} = 60 \text{ days} \quad \text{or, Debtors} = ₹12,82,192$$

(viii) Calculation of Long term Loan:

$$\frac{\text{Long term Loan}}{\text{Current Liabilities}} = \frac{2}{1} \quad \text{or, } \frac{\text{Long-term loan}}{₹11,00,000} = \frac{2}{1}$$

Or, Long-term loan = ₹ 22,00,000

(ix) Calculation of Cash Balance:

		(₹)
Current assets		22,00,000
Less: Debtors	12,82,192	
Raw materials stock	3,31,500	
Finished goods stock	3,97,800	(20,11,492)
Cash balance		1,88,508

(x) Calculation of Net worth:

Fixed Assets	26,00,000
Current Assets	22,00,000
Total Assets	48,00,000

Less: Long term Loan	22,00,000	
Current Liabilities	11,00,000	(33,00,000)
Net worth		15,00,000

Net worth = Share capital + Reserves and Surplus = ₹ 15, 00,000

$\frac{\text{Share Capital}}{\text{Reserve and Surplus}} = \frac{1}{4}$ or, Share Capital = 15,00,000 × $\frac{1}{5}$ = ₹ 3,00,000

Reserves and Surplus = 15,00,000 × $\frac{4}{5}$ = ₹ 12,00,000

Profit and Loss Account of PQR Ltd. for the year ended 31st December, 2015

Particulars	(₹)	Particulars	(₹)
To Direct Materials	13,26,000	By Sales	78,00,000
To Direct Wages	6,63,000		
To Works (Overhead) Balancing figure	46,41,000		
To Gross Profit c/d (15% of Sales)	11,70,000		
	78,00,000		78,00,000
To Operating and Selling & Distribution Expenses (Balancing figure)	5,46,000	By Gross Profit b/d	11,70,000
To Net Profit (8% of Sales)	6,24,000		
	11,70,000		11,70,000

Balance Sheet of PQR Ltd. as at 31st December, 2015

Liabilities	(₹)	Assets	(₹)
Share Capital	3,00,000	Fixed Assets	26,00,000
Reserves and Surplus	12,00,000	Current Assets:	
Long term loans	22,00,000	Stock of Raw Material	3,31,500
Current liabilities	11,00,000	Stock of Finished Goods	3,97,800
		Debtors	12,82,192

		Cash	1,88,508
	48,00,000		48,00,000

Note: No. of days in a year has been taken as 365. If 360 days in a year is considered then debtors will be $₹78,00,000 \times \frac{60\,\text{days}}{360\,\text{days}}$ = ₹13,00,000 and accordingly cash balance will be: [₹22,00,000 – (₹13,00,000 + ₹3,31,500 + ₹3,97,800)] = ₹1,70,700

4. Determination of specific costs:

(i) Cost Debt (K_d) $= \dfrac{\text{Interest}(1-t)+\dfrac{(RV-NP)}{N}}{\dfrac{(RV+NP)}{2}} = \dfrac{₹11(1-0.35)+\dfrac{(₹100-₹96)}{10\,\text{years}}}{\dfrac{(₹100+₹96)}{2}}$

$= \dfrac{₹7.15+₹0.4}{₹98}$ = 0.077 or 7.70%

(ii) Cost of Preference Shares (K_p) $= \dfrac{PD+\dfrac{(RV-NP)}{N}}{\dfrac{(RV+NP)}{2}} = \dfrac{₹12+\dfrac{(₹100-₹95)}{10\,\text{years}}}{\dfrac{(₹100+₹95)}{2}}$

$= \dfrac{₹12+₹0.5}{₹97.5}$ = 0.1282 or 12.82%

(iii) Cost of Equity shares (K_e) $= \dfrac{D_1}{P_0}+G = \dfrac{₹2}{₹22-₹2}+0.07$ = 0.17 or 17%

I – Interest, t – Tax, RV- Redeemable value, NP- Net proceeds, N- No. of years, PD- Preference dividend, D_1- Dividend at the end of the year, P_0- Price of share (net)

Using these specific costs we can calculate WACC on the basis of book value and market value weights as follows:

(a) Weighted Average Cost of Capital (K_0) based on Book value weights

Source of capital	Book value (₹)	Weights	Specific cost (%)	WACC (%)
Debentures	8,00,000	0.40	7.70	3.08
Preference shares	2,00,000	0.10	12.82	1.28

Equity shares	10,00,000	0.50	17.00	8.50
	20,00,000	1.00		12.86

(b) Weighted Average Cost of Capital (K_0) based on market value weights:

Source of capital	Market value (₹)	Weights	Specific cost (%)	WACC (%)
Debentures $\left(\frac{₹8,00,000}{₹100} \times ₹110\right)$	8,80,000	0.265	7.70	2.04
Preferences shares $\left(\frac{₹2,00,000}{₹100} \times ₹120\right)$	2,40,000	0.072	12.82	0.92
Equity shares $\left(\frac{₹10,00,000}{₹10} \times ₹22\right)$	22,00,000	0.663	17.00	11.27
	33,20,000	1.000		14.23

5. Ascertainment of probable price of shares of Akash limited

Particulars	Plan-I	Plan-II
	If ₹ 4,00,000 is raised as debt (₹)	If ₹ 4,00,000 is raised by issuing equity shares (₹)
Earnings Before Interest and Tax (EBIT) {20% of new capital i.e. 20% of (₹14,00,000 + ₹4,00,000)} (Refer working note1)	3,60,000	3,60,000
Less: Interest on old debentures (10% of ₹4,00,000)	(40,000)	(40,000)
Less: Interest on new debt (12% of ₹4,00,000)	(48,000)	--
Earnings Before Tax (EBT)	2,72,000	3,20,000
Less: Tax @ 50%	(1,36,000)	1,60,000
Earnings for equity shareholders (EAT)	1,36,000	1,60,000
No. of Equity Shares (refer working note 2)	30,000	40,000

Earnings per Share (EPS)	₹ 4.53	₹ 4.00
Price/ Earnings (P/E) Ratio (refer working note 3)	8	10
Probable Price Per Share (PE Ratio × EPS)	₹ 36.24	₹ 40

Working Notes:

1. **Calculation of existing Return of Capital Employed (ROCE):**

	(₹)
Equity Share capital (30,000 shares × ₹10)	3,00,000
10% Debentures $\left(₹40{,}000 \times \frac{100}{10}\right)$	4,00,000
Reserves and Surplus	7,00,000
Total Capital Employed	14,00,000
Earnings before interest and tax (EBIT) (given)	2,80,000
ROCE = $\frac{₹2{,}80{,}000}{₹14{,}00{,}000} \times 100$	20%

2. **Number of Equity Shares to be issued in Plan-II:**

$$= \frac{₹\,4{,}00{,}000}{₹\,40} = 10{,}000 \text{ shares}$$

Thus, after the issue total number of shares = 30,000+ 10,000 = 40,000 shares

3. **Debt/Equity Ratio if ₹ 4,00,000 is raised as debt:**

$$= \frac{₹8{,}00{,}000}{₹18{,}00{,}000} \times 100 = 44.44\%$$

As the debt equity ratio is more than 40% the P/E ratio will be brought down to 8 in Plan-I

6. Total Assets = ₹ 400 crores

Asset Turnover Ratio = 2.5

Hence, Total Sales = 400 × 2.5 = ₹ 1,000 crores

Computation of Profits after Tax (PAT)

	(₹ in crore)
Sales	1,000
Less: Variable operating cost (65% of ₹1,000 crore)	(650)
Contribution	350
Less: Fixed cost (other than Interest)	(80)
EBIT	270
Less: Interest on debentures (15% × ₹200 crore)	(30)
EBT	240
Less: Tax 40%	(96)
EAT (earnings available to equity share holders)	144

(i) Earnings per share (EPS)

$$\therefore \text{ EPS} = \frac{\text{₹ 144 crores}}{\text{10 crore equity shares}} = \text{₹ } 14.40$$

(ii) Operating Leverage

$$\text{Operating leverage} = \frac{\text{Contribution}}{\text{EBIT}} = \frac{350}{270} = 1.296$$

It indicates sensitivity of earnings before interest and tax (EBIT) to change in sales at a particular level.

(iii) Financial Leverage

$$\text{Financial Leverage} = \frac{\text{EBIT}}{\text{EBT}} = \frac{270}{240} = 1.125$$

The financial leverage is very comfortable since the debt service obligation is small vis-à-vis EBIT.

(iv) Combined Leverage

$$\text{Combined Leverage} = \frac{\text{Contribution}}{\text{EBIT}} \times \frac{\text{EBIT}}{\text{EBT}}$$

Or, Operating Leverage × Financial Leverage = 1.296 × 1.125 = 1.458

The combined leverage studies the choice of fixed cost in cost structure and choice of debt in capital structure. It studies how sensitive the change in EPS is vis-à-vis change in sales.

7. (i) Net Cash Outlay of New Machine

Purchase Price	₹ 60,00,000
Less: Exchange value of old machine	
[₹2,50,000 – 0.4 (₹2,50,000 – 0)]	1,50,000
	₹ 58,50,000

Depreciation base: Old machine has been fully depreciated for tax purpose.

Thus the depreciation base of the new machine will be its original cost i.e. ₹ 60,00,000.

Net Cash Flows: Unit cost includes depreciation and allocated overheads. Allocated overheads are allocations from corporate office therefore they are irrelevant. The depreciation tax shield may be computed separately. Excluding depreciation and allocated overheads, unit costs can be calculated. The company will obtain additional revenue from additional 20,000 units sold.

Thus, after-tax saving, excluding depreciation, tax shield, would be:

= (EBT under new machine – EBT under existing machine) × (1 - tax rate)

= {100,000 units (₹200 – ₹148*) – 80,000 units (₹200 – ₹173*)} × (1 – 0.40)

= {₹ 52,00,000 – ₹ 21,60,000} × 0.60 = ₹18,24,000

(* Excluding depreciation and allocated overheads)

After adjusting depreciation tax shield and salvage value, net cash flows and net present value are estimated.

Calculation of Cash flows and Project Profitability:

						(₹ '000)
	0	**1**	**2**	**3**	**4**	**5**
1. After-tax savings	-	1,824	1,824	1,824	1,824	1,824
2. Depreciation (₹60,00,000 - ₹ 2,50,000)/5	-	1,150	1,150	1,150	1,150	1,150
3. Tax shield on depreciation (Depreciation × Tax rate)	-	460	460	460	460	460
4. Net cash flows from operations (1+3)*	-	2,284	2,284	2,284	2,284	2,284
5. Initial cost	(5,850)					
6. Net Salvage Value (₹2,50,000 – ₹35,000)	-	-	-	-	-	215

7. Net Cash Flows (4 + 5 + 6)	(5,850)	2,284	2,284	2,284	2,284	2,499
8. PVF at 15%	1.00	0.8696	0.7561	0.6575	0.5718	0.4972
9. PV	(5,850)	1,986.166	1,726.932	1,501.73	1,305.99	1,242.50
10. NPV	1,913.32					

* Alternately Net Cash flows from operation can be calculated as follows:

Profit before depreciation and tax:

= 1,00,000 (₹200 - ₹148) - 80,000 (₹200 - ₹173) = ₹ 52,00,000 – ₹ 21,60,000

= ₹ 30,40,000

So, Profit after depreciation and tax is:

(₹30,40,000 - ₹11,50,000) × (1 - 0.40) = ₹ 11,34,000

So, Profit before depreciation and after tax is :

₹ 11,34,000 + ₹11,50,000 (Depreciation added back) = ₹ 22,84,000

(ii)

						(₹ '000)
	0	**1**	**2**	**3**	**4**	**5**
NCF	(5,850)	2,284	2,284	2,284	2,284	2,499
PVF at 20%	1.00	0.8333	0.6944	0.5787	0.4823	0.4019
PV	(5,850)	1,903.257	1,586.01	1,321.751	1,101.57	1,004.35
PV of benefits	6,916.94					
PVF at 30%	1.00	0.7692	0.5917	0.4552	0.3501	0.2693
PV	(5,850)	1,756.85	1,351.44	1,039.22	799.63	672.98
PV of benefits	5,620.12					

$$\text{IRR} = 20\% + 10\% \times \frac{1{,}066.94}{1{,}296.82} = 28.23\%$$

(iii) Advise: The Company should go ahead with replacement project, since it is positive NPV decision.

(Note: *Market Value of Old Machine:* The old machine could be sold for ₹ 1,50,000 in the market. Since the exchange value is more than the market value, this option is not attractive. This opportunity will be lost whether the old machine is retained or replaced. Thus, on incremental basis, it has no impact.)

8. (i) Statement showing Working Capital Investment for each policy

(₹ in crore)

	Working Capital Policy		
	Conservative	**Moderate**	**Aggressive**
Current Assets: (i)	4.50	3.90	2.60
Fixed Assets: (ii)	2.60	2.60	2.60
Total Assets: (iii)	7.10	6.50	5.20
Current liabilities: (iv)	2.34	2.34	2.34
Net Worth: (v) = (iii) - (iv)	4.76	4.16	2.86
Total liabilities: (iv) + (v)	7.10	6.50	5.20
Estimated Sales: (vi)	12.30	11.50	10.00
EBIT: (vii)	1.23	1.15	1.00
(a) Net working capital position: (i) - (iv)	2.16	1.56	0.26
(b) Rate of return: (vii) /(iii)	17.32%	17.69%	19.23%
(c) Current ratio: (i)/ (iv)	1.92	1.67	1.11

(ii) Statement Showing Effect of Alternative Financing Policy

(₹ in crore)

Financing Policy	**Conservative**	**Moderate**	**Aggressive**
Current Assets (i)	3.90	3.90	3.90
Fixed Assets (ii)	2.60	2.60	2.60
Total Assets (iii)	6.50	6.50	6.50
Current Liabilities (iv)	2.34	2.34	2.34
Short term Debt (v)	0.54	1.00	1.50
Total current liabilities (vi) = (iv) + (v)	2.88	3.34	3.84
Long term Debt (vii)	1.12	0.66	0.16
Equity Capital (viii)	2.50	2.50	2.50
Total liabilities (ix) = (vi)+(vii)+(viii)	6.50	6.50	6.50
Forecasted Sales	11.50	11.50	11.50
EBIT (x)	1.15	1.15	1.15
Less: Interest on short-term debt	0.06 (12% of ₹0.54)	0.12 (12% of ₹ 1)	0.18 (12% of ₹ 1.5)

Interest on long term debt	0.18 (16% of ₹1.12)	0.11 (16% of ₹0.66)	0.03 (16% of ₹0.16)
Earnings before tax (EBT) (xi)	0.91	0.92	0.94
Taxes @ 35% (xii)	0.32	0.32	0.33
Earnings after tax: (xiii) = (xi) – (xii)	0.59	0.60	0.61
(a) Net Working Capital Position: (i) - [(iv) + (v)]	1.02	0.56	0.06
(b) Rate of return on shareholders Equity capital : (xiii)/ (viii)	23.6%	24.0%	24.4%
(c) Current Ratio (i) / (vi)	1.35	1.17	1.02

9. (a) **Functions of Finance Manager**

The Finance Manager's main objective is to manage funds in such a way so as to ensure their optimum utilisation and their procurement in a manner that the risk, cost and control considerations are properly balanced in a given situation. To achieve these objectives the Finance Manager performs the following functions:

(i) *Estimating the requirement of Funds:* Both for long-term purposes i.e. investment in fixed assets and for short-term i.e. for working capital. Forecasting the requirements of funds involves the use of techniques of budgetary control and long-range planning.

(ii) *Decision regarding Capital Structure:* Once the requirement of funds has been estimated, a decision regarding various sources from which these funds would be raised has to be taken. A proper balance has to be made between the loan funds and own funds. He has to ensure that he raises sufficient long term funds to finance fixed assets and other long term investments and to provide for the needs of working capital.

(iii) *Investment Decision:* The investment of funds, in a project has to be made after careful assessment of various projects through capital budgeting. Assets management policies are to be laid down regarding various items of current assets. For e.g. receivable in coordination with sales manager, inventory in coordination with production manager.

(iv) *Dividend decision:* The finance manager is concerned with the decision as to how much to retain and what portion to pay as dividend depending on the company's policy. Trend of earnings, trend of share market prices, requirement of funds for future growth, cash flow situation etc., are to be considered.

(v) *Evaluating financial performance:* A finance manager has to constantly review the financial performance of the various units of organisation generally in terms of ROI Such a review helps the management in seeing how the funds have been utilised in various divisions and what can be done to improve it.

(vi) *Financial negotiation:* The finance manager plays a very important role in carrying out negotiations with the financial institutions, banks and public depositors for raising of funds on favourable terms.

(vii) *Cash management:* The finance manager lays down the cash management and cash disbursement policies with a view to supply adequate funds to all units of organisation and to ensure that there is no excessive cash.

(viii) K*eeping touch with stock exchange:* Finance manager is required to analyse major trends in stock market and their impact on the price of the company share.

(b) Inter-relationship between Investment, Financing and Dividend Decisions

The finance functions are divided into three major decisions, viz., investment, financing and dividend decisions. It is correct to say that these decisions are inter-related because the underlying objective of these three decisions is the same, i.e. maximisation of shareholders' wealth. Since investment, financing and dividend decisions are all interrelated, one has to consider the joint impact of these decisions on the market price of the company's shares and these decisions should also be solved jointly. The decision to invest in a new project needs the finance for the investment. The financing decision, in turn, is influenced by and influences dividend decision because retained earnings used in internal financing deprive shareholders of their dividends. An efficient financial management can ensure optimal joint decisions. This is possible by evaluating each decision in relation to its effect on the shareholders' wealth.

The above three decisions are briefly examined below in the light of their inter-relationship and to see how they can help in maximising the shareholders' wealth i.e. market price of the company's shares.

Investment decision: The investment of long term funds is made after a careful assessment of the various projects through capital budgeting and uncertainty analysis. However, only that investment proposal is to be accepted which is expected to yield at least so much return as is adequate to meet its cost of financing. This have an influence on the profitability of the company and ultimately on its wealth.

Financing decision: Funds can be raised from various sources. Each source of funds involves different issues. The finance manager has to maintain a proper balance between long-term and short-term funds. With the total volume of long-term funds, he has to ensure a proper mix of loan funds and owner's funds. The optimum financing mix will increase return to equity shareholders and thus maximise their wealth.

Dividend decision: The finance manager is also concerned with the decision to pay or declare dividend. He assists the top management in deciding as to what portion of the profit should be paid to the shareholders by way of dividends and what portion should be retained in the business. An optimal dividend pay-out ratio maximises shareholders' wealth.

The above discussion makes it clear that investment, financing and dividend decisions are interrelated and are to be taken jointly keeping in view their joint effect on the shareholders' wealth.

(c) **Debt Securitisation:** It is a method of recycling of funds. It is especially beneficial to financial intermediaries to support the lending volumes. Assets generating steady cash flows are packaged together and against this asset pool, market securities can be issued, e.g. housing finance, auto loans, and credit card receivables.

Process of Debt Securitisation

(i) *The origination function* – A borrower seeks a loan from a finance company, bank. The credit worthiness of borrower is evaluated and contract is entered into with repayment schedule structured over the life of the loan.

(ii) *The pooling function* – Similar loans on receivables are clubbed together to create an underlying pool of assets. The pool is transferred in favour of Special purpose Vehicle (SPV), which acts as a trustee for investors.

(iii) *The securitisation function* – SPV will structure and issue securities on the basis of asset pool. The securities carry a coupon and expected maturity which can be asset-based/mortgage based. These are generally sold to investors through merchant bankers. Investors are – pension funds, mutual funds, insurance funds.

PAPER – 4: TAXATION

PART – I: STATUTORY UPDATE

Significant Notifications and Circulars in income-tax and indirect taxes issued between 1st May, 2015 and 31st October, 2015

A. INCOME TAX

I. NOTIFICATIONS

1. Notification of Cost Inflation Index for Financial Year 2015-16 [Notification No. 60/2015, dated 24.7.2015]

Clause (v) of Explanation to section 48 defines "Cost Inflation Index", in relation to a previous year, to mean such Index as the Central Government may, by notification in the Official Gazette, specify in this behalf, having regard to 75% of average rise in the Consumer Price Index (Urban) for the immediately preceding previous year to such previous year.

Accordingly, the Central Government has, in exercise of the powers conferred by clause (v) of Explanation to section 48, specified the Cost Inflation Index for the **financial year 2015-16 as 1081**.

S. No.	Financial Year	Cost Inflation Index	S. No.	Financial Year	Cost Inflation Index
1.	1981-82	100	19.	1999-2000	389
2.	1982-83	109	20.	2000-01	406
3.	1983-84	116	21.	2001-02	426
4.	1984-85	125	22.	2002-03	447
5.	1985-86	133	23.	2003-04	463
6.	1986-87	140	24.	2004-05	480
7.	1987-88	150	25.	2005-06	497
8.	1988-89	161	26.	2006-07	519
9.	1989-90	172	27.	2007-08	551
10.	1990-91	182	28.	2008-09	582
11.	1991-92	199	29.	2009-10	632
12.	1992-93	223	30.	2010-11	711
13.	1993-94	244	31.	2011-12	785
14.	1994-95	259	32.	2012-13	852
15.	1995-96	281	33.	2013-14	939
16.	1996-97	305	34.	2014-15	1024
17.	1997-98	331	**35.**	**2015-16**	**1081**
18.	1998-99	351			

2. Basis for determining the period of stay in India for an Indian citizen, being a member of the crew of a foreign bound ship leaving India [Notification No. 70/2015, dated 17.8.2015]

Section 6(1) of the Income-tax Act, 1961 provides that an individual is said to be resident in India in any previous year, if he—

(a) is in India in that year for a period or periods amounting in all to 182 days or more; or

(c) having within the four years preceding that year been in India for a period or periods amounting in all to 365 days or more, is in India for a period or periods amounting in all to 60 days or more in that year.

However, where an Indian citizen leaves India as a member of crew of an Indian ship or for the purpose of employment outside India, he will be resident only if he stayed in India for 182 days during the previous year.

Thus, under section 6(1), the conditions to be satisfied by an individual to be a resident in India are provided. The residential status is determined on the basis of the **number of days of his stay in India** during a previous year.

However, in case of foreign bound ships where the destination of the voyage is outside India, there is uncertainty regarding the manner and the basis of determining the period of stay in India for an Indian citizen, being a crew member.

To remove this uncertainty, **Explanation 2 has been inserted to section 6(1)** to provide that in the case of an individual, being a citizen of India and a member of the crew of a foreign bound ship leaving India, the **period or periods of stay in India** shall, in respect of such voyage, be determined in the **prescribed manner** and subject to the prescribed conditions.

Accordingly, the CBDT has, in exercise of the powers conferred by Explanation 2 to section 6(1) read with section 295, vide this notification, with retrospective effect from 1st April, 2015, inserted Rule 126 in the Income-tax Rules, 1962, to compute the period of stay in such cases.

According to Rule 126, in case of an individual, being a citizen of India and a member of the crew of a ship, the **period or periods of stay in India** shall, in respect of an eligible voyage, **not include** the period **commencing from the date** entered into the Continuous Discharge Certificate in respect of **joining the ship** by the said individual for the eligible voyage and **ending on the date** entered into the Continuous Discharge Certificate in respect of **signing off by that individual from the ship** in respect of such voyage.

The Explanation to this Rule defines the meaning of the following terms:

Terms	Meaning
Continuous Discharge Certificate	This term has the meaning assigned to it in the Merchant Shipping (Continuous Discharge Certificate-cum-Seafarer's Identity Document) Rules, 2001 made under the Merchant Shipping Act, 1958.

Eligible voyage	A voyage undertaken by a ship engaged in the carriage of passengers or freight in international traffic where- (i) for the voyage having originated from any port in India, has as its destination any port outside India; and (ii) for the voyage having originated from any port outside India, has as its destination any port in India.

3. Certain districts of Bihar notified as backward areas under the first proviso to section 32(1)(iia) and section 32AD(1) [Notification No. 71/2015, dated 17.8.2015]

In order to encourage the setting up of industrial undertakings in the backward areas of the States of Andhra Pradesh, Bihar, Telangana and West Bengal, section 32AD(1) provides for a deduction of an amount equal to 15% of the actual cost of new plant and machinery acquired and installed in the assessment year relevant to the previous year in which such plant and machinery is installed, if the following conditions are satisfied by the assessee–

(a) the assessee sets up an undertaking or enterprise for manufacture or production of any article or thing on or after 1st April, 2015 in any backward area notified by the Central Government in the State of Andhra Pradesh or Bihar or Telangana or West Bengal; and

(b) the assessee acquires and installs new plant and machinery for the purposes of the said undertaking or enterprise during the period between 1st April, 2015 and 31st March, 2020 in the said backward areas.

Further, in order to encourage acquisition and installation of plant and machinery for setting up of manufacturing units in the notified backward areas of the States of Andhra Pradesh, Bihar, Telangana and West Bengal, first proviso has been inserted to section 32(1)(iia) to allow higher additional depreciation at the rate of 35% (instead of 20%) in respect of the actual cost of new machinery or plant (other than a ship and aircraft) acquired and installed during the period between 1st April, 2015 and 31st March, 2020 by a manufacturing undertaking or enterprise which is set up in the notified backward areas of these specified States on or after 1st April, 2015.

Accordingly, the Central Government has, vide this notification, notified the following **21 districts of the State of Bihar** as backward areas under the first proviso to section 32(1)(iia) and section 32AD(1).

S. No.	District	S. No.	District
1.	Patna	12.	Samastipur
2.	Nalanda	13.	Darbhanga
3.	Bhojpur	14.	Madhubani
4.	Rohtas	15.	Purnea

5.	Kaimur	16.	Katihar
6.	Gaya	17.	Araria
7.	Jehanabad	18.	Jamui
8.	Aurangabad	19.	Lakhisarai
9.	Nawada	20.	Supaul
10.	Vaishali	21.	M uzaffarpur
11.	Sheohar		

4. News agency notified for the purpose of section 10(22B) [Notification No. 72/2015, dated 24.8.2015]

Section 10(22B) provides that any income of a news agency set up in India solely for collection and distribution of news as the Central Government may notify shall be exempt, subject to the condition that such news agency applies its income or accumulates it for application solely for collection and distribution of news and does not distribute its income in any manner to its members.

Accordingly, the Central Government has, through this notification, specified the **Press Trust of India Limited, New Delhi** as a news agency set up in India solely for collection and distribution of news, for the purpose of section 10(22B) for three assessment years 2016-17 to 2018-19. The income of such news agency will not be included in computing the total income of a previous year of such agency, for three years, provided it applies its income or accumulates it for application solely for collection and distribution of news and does not distribute its income in any manner to its members.

5. Exemption in respect of transport allowance under Rule 2BB extended to deaf and dumb employees [Notification No. 75/2015, dated 23.09.2015]

The CBDT has, in exercise of the powers conferred by section 295 read with section 10(14), amended Rule 2BB which, *inter alia,* provides the limit of exemption of up to ₹ 1,600 p.m., in respect of transport allowance granted to an employee and up to ₹ 3,200 p.m., for an employee who is blind or orthopedically handicapped, with disability of lower extremities, to meet his expenditure incurred thereof, for the purpose of commuting between the place of his residence and the place of his duty.

Consequent to the amendment made vide this notification, the exemption up to ₹ 3,200 p.m. in respect of transport allowance can be claimed by a blind ***or deaf and dumb*** or orthopedically handicapped employee with disability of lower extremities to meet his expenditure for the purpose of commuting between the place of his residence and the place of his duty.

II. CIRCULARS

1. Tax not to be deducted from payments made to Corporations whose income is exempt under section 10(26BBB) [Circular No. 7/2015, dated 23-04-2015]

The CBDT had earlier issued Circular No. 4/2002 dated 16.07.2002 which laid down that there would be no requirement for tax deduction at source from payments made to such entities, whose income is unconditionally exempt under section 10 and who are statutorily not required to file return of income as per the section 139.

Section 10(26BBB), inserted by the Finance Act, 2003 w.e.f. 01.04.2004, exempts any income of a corporation established by a Central, State or Provincial Act for the welfare and economic up liftment of ex-service-men being the citizen of India. The corporations covered under section 10(26BBB) are also statutorily not required to file return of income as per the section 139.

Now, the CBDT has, vide this circular, clarified that since corporations covered under section 10(26BBB) satisfy the two conditions of Circular No. 4/2002 i.e., unconditional exemption of income under section 10 and no statutory liability to file return of income under section 139, they would also be entitled for the benefit of the said circular.

Hence, there would be no requirement for tax deduction at source from the payments made to such corporations since their income is anyway exempt under section 10.

2. Deduction in respect of cost of production allowable under section 37 in the case of Abandoned Feature Films [Circular No. 16/2015, dated 6.10.2015]

The deduction in respect of the cost of production of a feature film certified for release by the Board of Film Censors in a previous year is provided in Rule 9A.

In the case of abandoned films, however, since certificate of Board of Film Censors is not received, in some cases no deduction was allowed by applying Rule 9A of the Rules or by treating the expenditure as capital expenditure.

The CBDT has examined the matter in light of judicial decisions on this subject. The order of the Hon'ble Bombay High Court dated 28.1.2015 in ITA 310 of 2013 in the case of *Venus Records and Tapes Pvt. Ltd.* on this issue has been accepted and the aforesaid disputed issue has not been further contested.

Consequently, it is clarified that Rule 9A does not apply to abandoned feature films and that the expenditure incurred on such abandoned feature films is not to be treated as a capital expenditure. **The cost of production of an abandoned feature film is to be treated as revenue expenditure and allowed as per the provisions of section 37 of the Income-tax Act, 1961.**

B. INDIRECT TAXES

Chapter-5: Exemptions and Abatements

1. **Services provided under the Power System Development Fund Scheme of the Ministry of Power exempted from service tax**

   Exemption from service tax has been granted to taxable services provided under the Power System Development Fund Scheme of the Ministry of Power by way of-

   (A) re-gasification of Liquefied Natural Gas (LNG) imported by the Gas Authority of India Limited (GAIL);

   (B) transportation of the incremental Re-gasified Liquefied Natural Gas (RLNG) (e-bid RLNG) to specified power generating companies or plants

   subject to fulfillment of certain conditions prescribed in the exemption notification.

   However, the exemption shall not be available if such RLNG and LNG are used for generation of electrical energy by captive generating plant as defined in section 2(8) of the Electricity Act, 2003.

   Further, the exemption shall be valid only till 31.03.2017.

   [Notification No. 17/2015 ST dated 19.05.2015]

2. **Yoga included in the definition of charitable activities**

   Mega Exemption *Notification No. 25/2012 ST dated 20.06.2012* exempts services by an entity registered under section 12AA of the Income-tax Act, 1961 by way of charitable activities.

   Activities relating to advancement of religion or spirituality are included in the definition of charitable activities. Now yoga has also been included therein. Thus, services relating to advancement of yoga provided by charitable entities registered under section 12AA of the Income-tax Act, 1961 will not be liable to service tax e.g., service tax will not be payable on fee charged for yoga camps conducted by charitable trusts.

   [Notification No. 20/2015 ST dated 21.10.2015]

3. **Services provided by (i) business facilitator/business correspondent with respect to Basic Savings Bank Deposit Accounts covered by Pradhan Mantri Jan Dhan Yojana and (ii) an intermediary to business facilitator/business correspondent with respect to such services, exempt from service tax**

   With a view to promote financial inclusion, Mega Exemption *Notification No. 25/2012 ST dated 20.06.2012* has been amended to exempt the services provided by a business facilitator or a business correspondent to a banking company with respect to Basic Savings Bank Deposit Accounts covered by Pradhan Mantri Jan Dhan Yojana (PMJDY) by way of account opening, cash deposits, cash withdrawals, obtaining e-life certificates and Aadhar seeding, in the rural area branches of banking companies, from service tax. Further, the services provided by any person as an intermediary to a business facilitator or a business correspondent with respect to the above mentioned services, have also been exempted from service tax.

For this purpose, Basic Savings Bank Deposit Account has been defined to mean a Basic Savings Bank Deposit Account opened under the guidelines issued by Reserve Bank of India relating thereto.

[Notification No. 20/2015 ST dated 21.10.2015]

4. 70% abatement available on ancillary services provided by a GTA in the course of transportation of goods

It has been clarified that ancillary services such as loading/ unloading, packing/unpacking, transshipment, temporary storage etc., would form part of the goods transport agency's (GTA) service if such services are provided by a GTA in the course of transportation of goods and the charges for such services are included in the invoice issued by the GTA, and not by any other person. Thus, abatement of 70%, applicable to GTA service, would also be available to the ancillary services. In other words, a single composite service need not be broken into its components and need not be considered as constituting separate services, if it is provided as such in the ordinary course of business. Thus, a composite service should be treated as a single service based on the main or principal service.

It has also been clarified that in cases where GTA undertakes to deliver goods at a destination within a stipulated time, it should be considered as services of GTA in relation to transportation of goods. Thus abatement of 70% will be applicable if the entire transportation of goods is by road and the GTA issues a consignment note, by whatever name called.

[Circular No. 186/5/2015 ST dated 05.10.2015]

Chapter 7: CENVAT Credit

5. No refund of CENVAT credit under rule 5B to service providers providing manpower supply/ security services

Rule 5B of the CENVAT Credit Rules, 2004 provides that service providers, rendering notified reverse charge services, being unable to utilise the CENVAT credit availed on inputs and input services for payment of service tax on such output services, shall be allowed refund of such unutilised CENVAT credit.

In this regard, earlier following partial reverse charge services were notified:

(i) renting of a motor vehicle designed to carry passengers on non-abated value, to any person who is not engaged in a similar business;

(ii) supply of manpower for any purpose or security services; or

(iii) service portion in the execution of a works contract

Since with effect from 01.04.2015, service tax with respect to supply of manpower for any purpose or security services is payable on the basis full reverse charge, service providers of said services will no longer be eligible for refund of CENVAT credit availed on inputs and input services for payment of service tax on such output services. Further, application in Form A for claiming refund has also been suitably modified.

The aforesaid amendment is effective from April 01, 2015.

[Notification No. 15/2015 CE (NT) dated 19.05.2015]

6. Reversal of credit under rule 6 not required in case of ethanol produced from molasses generated from cane crushed in the sugar season 2015-16 [Clause (ix) inserted to rule 6(6) of the CENVAT Credit Rules, 2004]

The provisions of sub-rules (1), (2), (3) and (4) of rule 6 would not apply to ethanol produced from molasses generated from cane crushed in the sugar season 2015-16 i.e. 1st October, 2015 onwards, for supply to the public sector oil marketing companies, namely, Indian Oil Corporation Ltd., Hindustan Petroleum Corporation Ltd. or Bharat Petroleum Corporation Ltd., for the purposes of blending with petrol, under *Notification No.12/2012 CE dated 17.03.2012*.

In case of such removal, though ethanol is removed without payment of duty, CENVAT credit on inputs/capital goods/input services used in the manufacture of ethanol can be availed. Further, where common inputs/input services are used to manufacture ethanol and other dutiable final product, reversal of credit or payment of amount on removal of ethanol will not be required.

[Notification No. 21/2015 CE (NT) dated 07.10.2015]

7. Output service providers allowed to utilize credit of education cess (EC) and secondary and higher education cess (SHEC) for payment of service tax on any output service [Sixth, seventh and eighth provisos inserted to rule 3(7)(b) of the CENVAT Credit Rules, 2004]

Prior to 01.03.2015, education cess (EC) and secondary and higher education cess (SHEC) paid on excisable goods could be availed as CENVAT credit. Further, EC and SHEC paid on taxable services could also be availed as CENVAT credit till 31.05.2015. Credit of EC on excisable goods or taxable services could not be utilised for payment of any other duty except EC payable on excisable goods or taxable services. Similarly, credit of SHEC on excisable goods or taxable services could not be utilised for payment of any other duty except SHEC payable on excisable goods or taxable services.

However, pursuant to EC and SHEC leviable on all taxable services ceasing to have effect (with effect from 01.06.2015), an output service provider has been allowed to utilise the following credits of EC and SHEC for the payment of service tax on any output service:

(i) credit of EC and SHEC paid on inputs/ capital goods received in the premises of the output service provider on or after 01.06.2015;

(ii) credit of balance 50% EC and SHEC paid on capital goods received in the premises of the output service provider in the financial year 2014-15; and

(iii) credit of EC and SHEC paid on input service in respect of which the invoice, bill, challan or Service Tax Certificate for Transportation of Goods by Rail (referred to in rule 9), as the case may be, is received by the output service provider on/ after 01.06.2015.

[Notification No. 22/2015 CE (NT) dated 29.10.2015]

8. Amount payable under rule 6(3)(i) of CENVAT Credit Rules, 2004 enhanced from 6% to 7% of the value of exempted services

Earlier, in case an output service provider provides output service chargeable to tax as well as exempted services, he had an option to avail CENVAT credit in respect of any inputs/ input services without maintaining separate accounts provided he has paid an amount equal to 6% of the value of exempted services [Rule 6(3)(i) of the CENVAT Credit Rules, 2004].

With effect from 01.06.2015, pursuant to increase in the rate of service tax from 12% to 14%, aforesaid rate has been enhanced from 6% to 7%. Further, if any part of the value of a taxable service has been exempted on the condition that no CENVAT credit of inputs and input services, used for providing such taxable service, shall be taken, amount specified in rule 6(3)(i) has also been enhanced to 7% of the value so exempted.

[Notification No. 14/2015 CE (NT) dated 19.05.2015]

PART – II: QUESTIONS AND ANSWERS

QUESTIONS

Residential Status and Scope of total income

1. State with reasons whether the following transactions attract income-tax in India in the hands of recipients for A.Y.2016-17:

(i) Post office savings bank interest of ₹ 15,000 received by a resident assessee, Mr. Pankaj.

(ii) Legal charges of ₹ 5,00,000 paid in Madras to a lawyer of Canada who visited India to represent a case at the Madras High Court.

(iii) Royalty paid by Mr. Harish, a resident, to Mr. Rajesh, a non-resident, in respect of a business carried on in France.

(iv) Salary paid by Central Government to Mr. Avi, a citizen of India ₹ 11,00,000 for the services rendered in USA.

Income which do not form part of total income

2. Mr. X, a sole proprietor, has one unit at Special Economic Zone (SEZ) and another unit at Domestic Tariff Area (DTA). The following are the details of the sole proprietorship for the previous year 2015-16.

Particulars	Mr. X (₹)	Unit in DTA (₹)
Total Sales	9,00,00,000	3,00,00,000
Export Sales	4,80,00,000	2,20,00,000
Net Profit	1,20,00,000	30,00,000

Calculate the eligible deduction under section 10AA of the Income-tax Act, 1961, for the Assessment Year 2016-17, in the following situations:

(i) If both the units were set up and start manufacturing from 18-08-2009.

(ii) If both the units were set up and start manufacturing from 23-09-2013.

Income from Salaries

3. Mr. Shyam is a Finance Executive at Xerox Ltd. From the following particulars, compute his total income for the Assessment Year 2016-17:

Basic salary	₹ 30,000 per month
Dearness allowance	30% of basic salary
Transport allowance (for commuting between place of residence and office)	₹ 1,800 per month
Motor car running and maintenance charges fully paid by employer	₹ 40,000
(The motor car is owned and driven by employee Shyam. The engine cubic capacity is below 1.60 litres. The motor car is used for both official and personal purpose by the employee)	
Expenditure on accommodation in hotels while touring on official duties met by the employer.	₹ 30,000
Lunch provided by the employer during office hours.	
Cost to the employer	₹ 12,000
Computer (cost ₹ 50,000) kept by the employer in the residence of Shyam from 1.10.2015	
Interest on saving bank account	₹ 12,000
Shyam made the following payments:	
Tuition fees for 2 children studying post-graduation courses at Madras University	₹ 1,60,000

Medical insurance premium : Paid by cash	₹ 5,000
Paid by cheque	₹ 22,000
Expenditure on preventive health checkup (incurred in cash)	₹ 7,000

Income from house property

4. Garima has two flats in Chennai, both of which are self-occupied. The particulars of these are given below:

	(Value in ₹)	
Particulars	**Flat at Adyar**	**Flat at Mylapore**
Municipal Valuation per annum	1,20,000	1,15,000
Fair Rent per annum	1,40,000	1,60,000
Standard rent per annum	1,20,000	1,70,000
Date of completion of construction	1-01-2009	21-05-2003
Municipal taxes payable during the year (paid for Flat at Mylapore only)	10%	12%
Interest on money borrowed for repair of property during current year	-	52,000

Compute Garima's income from house property for the Assessment Year 2016-17. Also, suggest which flat should be opted by Garima to be assessed as self-occupied so that her tax liability is minimum.

Profits and gains of business or profession

5. Discuss, on the basis of the provisions of Income-tax Act, 1961 as amended by the Finance Act, 2015, the correctness or otherwise of the following statements:

   (i) Where new plant and machinery acquired during the P.Y. 2015-16 is put to use for less than 180 days in that year, additional depreciation allowable under section 32(1)(iia) for A.Y.2016-17 is restricted to 10% (i.e., 50% of 20%). The balance additional depreciation cannot be claimed in future.

   (ii) A manufacturing company set up in Vaishali, a notified backward area in the State of Bihar, acquires and installs new plant and machinery for ₹ 30 crores in the P.Y. 2015-16. For A.Y.2016-17, it is entitled to deduction either under section 32AC or section 32AD, but not both.

   (iii) Interest paid in respect of capital borrowed for acquisition of an asset, for the period upto the date on which the asset is first put to use must not be capitalized, if the acquisition of the asset is not for extension of existing business or profession.

Capital Gains & Income from Other Sources

6. Mr. Sitesh sold a house to his friend Mr. Gautam on 21st December, 2015 for a consideration of ₹ 30,00,000. The Sub-Registrar refused to register the document for the said value, as according to him, stamp duty had to be paid on ₹ 52,00,000, which was the Government guideline value. Mr. Sitesh preferred an appeal to the Revenue Divisional Officer, who fixed the value of the house as ₹ 35,00,000 (₹ 25,00,000 for land and the balance for building portion). The differential stamp duty was paid, accepting the said value determined. What are the tax implications in the hands of Mr. Sitesh and Mr. Gautam for the assessment year 2016-17? Mr. Sitesh had purchased the land on 21st March, 2011 for ₹ 6,19,000 and completed the construction of house on 2nd January, 2014 for ₹ 12,50,000.

   Cost inflation indices may be taken as 711 for the financial year 2010-11, 939 for the financial year 2013-14 and 1081 for the financial year 2015-16.

Income of Other Persons included in assessee's Total Income

7. Mr. Chauhan commenced a proprietary business on 01.04.2014 with a capital of ₹ 10,00,000. He incurred a loss of ₹ 4,00,000 during the year 2014-15. To help her husband tide over the loss, his wife Mrs. Aparna, a Chartered Accountant, gave a gift of ₹ 4,00,000 on 01.04.2015, which was immediately invested in the business by Mr. Chauhan. He earned a profit of ₹ 5,00,000 during the year 2015-16. What is the amount to be clubbed in the hands of Mrs. Aparna for the Assessment Year 2016-17. Would your answer be different, if Mrs. Aparna gave the said amount as loan?

Set off and Carry Forward of Losses

8. Mr. Jain, a resident individual, furnishes the following particulars of his income and other details for the previous year 2015-16.

		₹
(1)	Income from Salary	70,000
(2)	Loss from house property (Computed)	25,000
(3)	Business loss	40,000
(4)	Long term capital gain on sale of land	82,700
(5)	Loss on maintenance of race horses	21,000
(6)	Loss from gambling	12,100

   The other details of unabsorbed depreciation and brought forward losses pertaining to Assessment Year 2015-16 are as follows:

		₹
(1)	Unabsorbed depreciation	20,000

(2)	Loss from Speculative business	22,000
(3)	Short term capital loss	9,700

Compute the Gross total income of Mr. Jain for the Assessment Year 2016-17 and the amount of loss, if any, that can be carried forward or not.

Deductions from Gross Total Income

9. Mr. Hariharan, working with Gamma Ltd., submits the following particulars of investments and payments made by during the previous year 2015-16:

- Deposit of ₹ 1,60,000 in public provident fund
- Payment of life insurance premium of ₹ 25,000 on the policy taken on 31.3.2012 to insure his life (Sum assured – ₹ 1,00,000).
- Deposit of ₹ 50,000 in a five year term deposit with bank.
- Contributed ₹ 2,10,000, being 15% of his salary, to the NPS of the Central Government. A matching contribution was made by Gamma Ltd.
- Paid mediclaim premium of ₹ 22,000 to insure his health and ₹ 26,000 to insure the health of his father, aged 65 years, not dependent on him.
- He spent ₹ 5,000 for the preventive health-check up of his wife and ₹ 5,000 for the preventive check up of his father.
- He has incurred an expenditure of ₹ 50,000 for the medical treatment of his mother, being a person with severe disability.

(i) Compute the deduction available to Mr. Hariharan under Chapter VI-A for A.Y.2016-17.

(ii) Would your answer be different, if Mr. Hariharan contributed ₹ 1,40,000 (being, 10% of his salary) towards NPS of the Central Government ?

Computation of total income and tax liability of an individual

10. Dr. Ashish Puri is running a clinic. His Income and Expenditure account for the year ending 31st March, 2016 is given below:

Expenditure	₹	Income	₹
To Staff Salary	4,30,000	By Fees Receipts	12,63,600
To Consumables	10,750	By Dividend from Indian Companies	15,000
To Medicine consumed	3,69,800	By Winning from Lotteries (Net of TDS of ₹ 12,000)	28,000
To Depreciation	91,000	By Income-tax refund	2,750

To Administrative Expenses	1,51,000		
To Donation to Prime Minister's National Relief Fund	5,000		
To Excess of Income over expenditure	2,51,800		
Total	**13,09,350**	**Total**	**13,09,350**

(i) Depreciation in respect of all assets has been ascertained at ₹ 50,000 as per Income-tax Rules, 1962.

(ii) Medicines consumed include medicine of (cost) ₹ 25,000 used for his family.

(iii) Fees Receipts include ₹ 20,000 honorarium for valuing medical examination answer books.

(iv) He has also received ₹ 2,75,000 on account of Agricultural Income which had not been included in the above Income and Expenditure Account.

(v) He has also received ₹ 62,000 on maturity of one LIC Policy, not included in the above Income and Expenditure Account.

(vi) He received ₹ 8,000 per month as salary from a City Care Centre. This has not been included in the 'Fees Receipts' credited to Income and Expenditure Account.

(vii) He has sold land in August, 2015 for ₹ 12,00,000 (valuation as per stamp valuation authority ₹ 14,00,000). The land was acquired by him in May, 1999 for ₹ 4,00,000.

(viii) He has paid premium of ₹ 45,000 for another LIC Policy on his life which was taken on 1.04.2013 (sum assured ₹ 5,00,000).

(ix) He has paid ₹ 4,000 for purchase of lottery tickets, which has not been debited to Income and Expenditure account.

(x) Donation to Prime Minister National Relief Fund has been made by way of an crossed cheque.

(xi) He deposited ₹ 1,50,000 in PPF.

From the above, compute the income and tax payable of Dr. Ashish Puri for the A.Y. 2016-17.

Cost Inflation Index: F.Y. 1999-00 – 389; F.Y. 2015-16 – 1081.

Provisions concerning Advance Tax and Tax Deducted at Source

11. Examine the implications of tax deduction at source under section 194A in the cases mentioned hereunder, based on the provisions of the Income-tax Act, 1961, as amended by the Finance Act, 2015 –

   (i) On 1.10.2015, Mr. Mohit made a six-month fixed deposit of ₹ 12 lakh @ 8% p.a. with Theta Co-operative Bank. The fixed deposit matures on 31.3.2016.

(ii) Mr. Harish made fixed deposits carrying interest @10% p.a. with the following branches of Omega Bank, a bank which has adopted CBS.

Branch	Amount (₹)	Date of deposit	Date of Maturity
Adyar	60,000	01.06.2015	31.03.2016
Anna Nagar	80,000	01.07.2015	31.03.2016
Nungambakkam	75,000	01.08.2015	31.03.2016

(iii) On 1.4.2015, Ms. Meena started a 1 year recurring deposit of ₹ 20,000 per month @ 10% p.a. with Gamma Bank. The recurring deposit matures on 31.3.2016.

Provisions for Filing of Return of Income

12. Explain with brief reasons whether the return of income can be revised under section 139(5) of the Income-tax Act, 1961 in the following cases:

(i) Belated return filed under section 139(4).

(ii) Return already revised once under section 139(5).

(iii) Return of loss filed under section 139(3).

Computation of assessable value and excise duty payable thereon

13. Super Lasting Ltd. sold a machine, manufactured by it, to Goel Steel Ltd. (GSL) at a price of ₹ 10,00,000 (excluding taxes and duties). Further, following additional amounts were also charged from GSL:

Particulars	(₹)
Outward handling charges (from factory to GSL's premises)	5,000
Protective packing charges	12,500
Expenses pertaining to installation and erection of the machine at premises of GSL (machine was permanently affixed to earth)	26,000
Testing and inspection charges (testing done by Super Lasting Ltd.)	40,000
Delayed payment charges	3,000
Dharmada (charged in the invoice and recovered from GSL)	10,000

Determine the assessable value and total amount of central excise duty payable on the machine from the aforesaid information assuming that the machinery has been sold at the factory gate.

Computation of customs duty

14. ABC Ltd. has imported a machinery to be used for providing a taxable service. The assessable value of imported machinery under customs laws is ₹ 2,00,000. Basic customs duty is payable @ 10%. If the machinery is manufactured in India, excise duty @ 12.5% is leviable on such machinery. Education cess and secondary and higher education cess of customs are as applicable. Special CVD is payable on said machinery @ 4%. You are required to:-

    (i) calculate the total customs duty payable.

    (ii) examine whether ABC Ltd. can avail any CENVAT credit of the custom duties so paid? If yes, how much?

Inter-State sales under CST

15. Examine whether the following amount to inter-State sales under CST:-

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

    (ii) M of Mumbai comes to Delhi, purchases certain chemicals from N and transports them in his own name to Mumbai.

    (iii) A London based entrepreneur enters into a contract of sale of goods with Pawan of Gujarat and sends the goods to India.

VAT liability

16. Mr. Naveen is a registered dealer of goods in Bihar. He sells his products to dealers in his State and in other States. Following additional information is provided by Mr. Naveen:

    (i) Raw material purchased in Bihar worth ₹ 80,000 (excluding VAT @ 12.5%)

    (ii) High seas purchases of raw materials are ₹ 1,85,000 (excluding custom duty @ 10%).

    (iii) Purchases of raw materials from West Bengal (excluding CST @ 2%) worth ₹ 50,000

    (iv) Transportation charges, wages and other manufacturing expenses are ₹ 3,50,000

    (v) Interest paid on bank loan is ₹ 55,000. Loan is taken to acquire a land for building a factory.

    Mr. Naveen has sold all the manufactured goods after adding a profit margin of 10% of cost of production. VAT rate on sales is 12.5%. You are required to compute net VAT liability and total sales value (invoice value). There is no opening or closing inventory of both raw materials and manufactured goods.

Basic concepts of service tax

17. With reference to the provisions of service tax law as amended by the Finance Act, 2015, briefly examine the service tax implications in the following independent cases:-

    (a) AB Pvt. Ltd. manufactures alcoholic liquor for human consumption on job-work basis.

    (b) Splash and Splutter is a water park. It charges ₹ 500 per person as entry fee.

Point of taxation

18. Softec Industries Ltd. (SIL) is an Indian Company. It has received management consultancy services from a UK based company-Mitchell Ltd. on 15.07.2015. Assuming that Mitchell Ltd. and SIL are associated enterprises, determine the point of taxation using following details:

Particulars	Date
Mitchell Ltd. raised on SIL an invoice of £ 58,000	27.07.2015
SIL debited its books of accounts	05.08.2015
Date of payment by SIL	24.09.2015

Valuation of taxable service

19. BIE Academy, registered as a company, is engaged in providing online coaching classes to students of Class XI and XII. During the year ended 31.03.2015, it paid a sum of ₹ 15.6 lakh as service tax, out of which ₹ 7,00,000 was paid by utilizing the CENVAT credit and balance was paid in cash on the respective due dates. The details pertaining to the month of July, 2015 are as under:

Particulars	₹
Free online access for coaching provided to a batch of 100 students (Value of similar services is ₹ 52,000)	
Advance fees collected from students for online coaching sessions to be held in August, 2015	12,00,000
Advance received on 31.07.2015 from ABC School for conducting online classes specially designed for their students, in November, 2015. However, due to some internal disagreement, ABC School cancelled the agreement on 12.08.2015. The advance received was forfeited by BIE Academy.	5,92,000

Determine the service tax liability of BIE Academy for the month of July, 2015.

Note: Wherever applicable, service tax has not been charged separately.

Exemptions under service tax

20. Examine the following independent services provided in the month of August, 2015 and determine the amount of service tax payable, if any, in each of these cases:

S. No.	Particulars	(₹)
1.	Services by way of waxing of apples to provide it an artificial sheen for increasing its marketability	1,00,000
2.	Admission to a Railway Museum	50,000
3.	Transportation of patients to ABC Nursing Home and Bheem Multispecialty Hospital, in an ambulance owned by XYZ Ltd.	1,20,000
4.	Admission to a Telly Award Function [Value per ticket per person is ₹ 510]	5,10,000
5.	Transportation of milk by a goods transport agency	1,50,000

Note: Ignore small service providers' exemption. Wherever applicable, service tax has been charged separately.

21. Kesar Maharaj, a renowned classical dancer gave a classical dance performance in an auditorium. The consideration charged for the said performance is ₹ 98,500. Is Kesar Maharaj liable to pay service tax on the consideration received for the said performance if such performance is not for promotion of any product/services? If yes, determine his service tax liability. Will your answer be different if:

    (i) consideration charged by Kesar Maharaj for the said performance is ₹ 1,20,000?

    (ii) Kesar Maharaj is a brand ambassador of a food product and aforesaid performance is for the promotion of such food product?

    (iii) Kesar Maharaj gives a contemporary Bollywood style dance performance?

    Note: Ignore small service providers' exemption. Wherever applicable, service tax has been charged separately.

Payment of service tax at alternative rates

22. Mr. Paritosh is an air travel agent. He is finding it difficult to charge service tax @ 14% on the value of services provided by him. Can Mr. Paritosh pay service tax at any alternative rate? Explain.

    Whether such option of payment of service tax at alternative rates is available in respect of any other service? If yes, mention such service(s).

CENVAT credit

23. "CENVAT credit of excise duty paid on inputs can be taken by a manufacturer or an output service provider only when the same are received in the factory or the premises of the output service provider."

Examine the validity of the statement.

24. LT Pvt. Ltd. manufactures rubber slippers. Compute the CENVAT credit available with LT Pvt. Ltd. in respect of the following goods/services procured by it:

S. No.	Particulars	Excise duty paid (₹)	Service tax paid (₹)
(i)	Machine for manufacture of rubber soles	10,00,000	
(ii)	Rubber sheets for manufacture of slippers	5,00,000	
(iii)	Adhesives	50,000	
(iv)	Club Membership fee of employees		1,00,000
(v)	Expenses incurred on advertising the slippers on television		5,00,000

Note: LT Pvt. Ltd. is not entitled to SSI exemption under Notification No. 8/2003 CE dated 01.03.2003.

SUGGESTED ANSWERS/HINTS

1.

	Taxable/Not Taxable	Amount liable to tax (₹)	Reason
(i)	Partly Taxable	1,500	The interest on Post Office Savings Bank Account, would be exempt under section 10(15)(i), only to the extent of ₹ 3,500 in case of an individual account. Hence, ₹ 11,500 will be taxable under the head "Income from other sources" and will form part of Gross Total Income. ₹ 10,000, however, would be allowed as deduction under section 80TTA from Gross Total Income.
(ii)	Taxable	5,00,000	In case of a non-resident, any income which accrues or arises in India or which is deemed to accrue or arise in India or which is received in India or is deemed to be received in India is taxable in India. Therefore, legal charges paid in India to a non-resident lawyer of Canada, who visited India to represent a case at the Madras High Court would be taxable in India.

(iii)	Not Taxable	-	Royalty paid by a resident to a non-resident in respect of a business carried in France, would not be taxable in the hands of the non-resident provided the same is not received in India. This has been provided as an exception to deemed accrual mentioned in section 9(1)(vi)(b).
(iv)	Taxable	11,00,000	As per section 9(1)(iii), salaries payable by the Government to a citizen of India for service rendered outside India shall be deemed to accrue or arise in India. Therefore, salary paid by Central Government to Mr. Avi for services rendered in USA would be deemed to accrue or arise in India, since he is a citizen of India.

2. Computation of deduction under section 10AA of the Income-tax Act, 1961

As per section 10AA, in computing the total income of Mr. X from its unit located in a Special Economic Zone (SEZ), which begins to manufacture or produce articles or things or provide any services during the previous year relevant to the assessment year commencing on or after 01.04.2006, there shall be allowed a deduction of 100% of the profit and gains derived from export of such articles or things or from services for a period of five consecutive assessment years beginning with the assessment year relevant to the previous year in which the Unit begins to manufacture or produce such articles or things or provide services, as the case may be, and 50% of such profits for further five assessment years subject to fulfillment of other conditions specified in section 10AA.

Computation of eligible deduction under section 10AA [See Working Note below]:

(i) <u>If Unit in SEZ was set up and began manufacturing from 18-08-2009:</u>

Since A.Y. 2016-17 is the 7th assessment year from A.Y. 2010-11, relevant to the previous year 2009-10, in which the SEZ unit began manufacturing of articles or things, it shall be eligible for deduction of 50% of the profits derived from export of such articles or things, assuming all the other conditions specified in section 10AA are fulfilled.

$$= \text{Profits of Unit in SEZ} \times \frac{\text{Export turnover of Unit in SEZ}}{\text{Total turnover of Unit in SEZ}} \times 50\%$$

$$= 90 \text{ lakhs} \times \frac{260 \text{ lakhs}}{600 \text{ lakhs}} \times 50\% = ₹\ 19.50 \text{ lakhs}$$

(ii) <u>If Unit in SEZ was set up and began manufacturing from 23-09-2013:</u>

Since A.Y.2016-17 is the 3rd assessment year from A.Y. 2014-15, relevant to the previous year 2013-14, in which the SEZ unit began manufacturing of articles or things, it shall be eligible for deduction of 100% of the profits derived from export of such articles or things, assuming all the other conditions specified in section 10AA are fulfilled.

$$= \text{Profits of Unit in SEZ} \times \frac{\text{Export turnover of Unit in SEZ}}{\text{Total turnover of Unit in SEZ}} \times 100\%$$

$$= 90 \text{ lakhs} \times \frac{260 \text{ lakhs}}{600 \text{ lakhs}} \times 100\% \qquad = ₹\ 39 \text{ lakhs}$$

The unit set up in Domestic Tariff Area is not eligible for the benefit of deduction under section 10AA in respect of its export profits, in both the situations.

Working Note:

Computation of total sales, export sales and net profit of unit in SEZ

Particulars	Mr. X (₹)	Unit in DTA (₹)	Unit in SEZ (₹)
Total Sales	9,00,00,000	3,00,00,000	6,00,00,000
Export Sales	4,80,00,000	2,20,00,000	2,60,00,000
Net Profit	1,20,00,000	30,00,000	90,00,000

3. **Computation of taxable income of Mr. Shyam for the A.Y. 2016-17**

Particulars	₹	₹
<u>Income from salary</u>		
Basic salary (₹ 30,000 x 12)		3,60,000
Dearness allowance @ 30%		1,08,000
Transport allowance (₹ 1800 x 12)	21,600	
Less: Exemption under section 10(14) (read with Rule 2BB @ ₹ 1,600 p.m.)	19,200	2,400
Motor car maintenance borne by employer [₹ 40,000 - ₹ 21,600 (i.e., ₹ 1,800 × 12)]		18,400
Expenditure on accommodation while on official duty not a perquisite and hence not chargeable to tax		Nil
Value of lunch provided during working hours (not chargeable to tax as per Rule 3(7)(iii)-free food provided by the employer during working hours is not treated as perquisite provided that the value thereof does not exceed fifty rupees per meal)		Nil
Computer provided in the residence of employee by the employer – not chargeable to tax [Rule 3(7)(vii)]		Nil

Income from other sources		
Interest on saving bank account		12,000
Gross Salary		**5,00,800**
Less: Deduction under Chapter VI-A		
Under section 80C		
Tuition fees paid for two children ₹ 1,60,000		
Restricted to		1,50,000
Under section 80D		
Medical insurance premium otherwise than by way of cash would only be allowed as deduction. Hence, only premium paid by cheque would be deductible	22,000	
Expenditure on Preventive health checkup restricted to ₹ 5,000 (payment made in cash would also qualify for deduction)	5,000	
	27,000	
Restricted to overall limit of		25,000
Under section 80TTA		
Interest on saving bank account ₹ 12,000, subject to a limit of ₹ 10,000		10,000
Total income		**3,15,800**

4. In this case, Garima has more than one house property for self-occupation. As per section 23(4), Garima can avail the benefit of self-occupation (i.e., benefit of "Nil" Annual Value) only in respect of one of the house properties, at her option. The other house property would be treated as "deemed let-out" property, in respect of which the expected rent would be the gross annual value. Garima should, therefore, consider the most beneficial option while deciding which flat should be treated by her as self-occupied.

OPTION 1 [Flat at Adyar – Self-occupied and Flat at Mylapore – Deemed to be let out]

If Flat at Adyar is opted to be self-occupied, Garima's income from house property for A.Y.2016-17 would be –

Particulars	Amount in ₹
Flat at Adyar (Self-occupied) [Annual value is Nil]	Nil
Flat at Mylapore (Deemed to be let-out) ***[See Working Note below]***	50,340
Income from house property	**50,340**

OPTION 2 [Flat at Adyar – Deemed to be let out and Flat at Mylapore – Self-occupied]

If Flat at Mylapore is opted to be self-occupied, Garima's income from house property for A.Y.2016-17 would be –

Particulars	Amount in ₹
Flat at Adyar (Deemed to be let-out) ***[See Working Note below]***	84,000
Flat at Mylapore (Self-occupied) [Annual value is Nil, but interest deduction would be available, subject to a maximum of ₹ 30,000. In case of money borrowed for **repair of self-occupied property**, the interest deduction would be restricted to ₹ 30,000, irrespective of the date of borrowal].	(30,000)
Income from house property	**54,000**

Since Option 1 is more beneficial, Garima should opt to treat Flat at Adyar as Self-occupied and Flat at Mylapore as Deemed to be let out, in which case, her income from house property would be ₹ 50,340 for the A.Y. 2016-17.

Working Note:

Computation of income from Flats at Adyar & Mylapore assuming that both are deemed to be let out

Particulars	Amount in Rupees	
	Flat at Adyar	**Flat at Mylapore**
Gross Annual Value (GAV)		
Expected Rent is the GAV of house property		
Expected Rent = Higher of Municipal Value and Fair Rent but restricted to Standard Rent	1,20,000	1,60,000
Less: Municipal taxes (paid by the owner during the previous year)	Nil	13,800
Net Annual Value (NAV)	**1,20,000**	**1,46,200**
Less: **Deductions under section 24**		
(a) 30% of NAV	36,000	43,860
(b) Interest on borrowed capital (allowed in full in case of deemed let out property)	-	52,000
Income from deemed to be let-out house property	**84,000**	**50,340**

5. (i) **The statement is not correct.**

As per the third proviso to section 32(1)(ii), 50% of the additional depreciation on new plant and machinery acquired and used for less than 180 days in the year of acquisition and installation which has not been allowed as deduction in that previous year, shall be allowed in the immediately succeeding previous year.

Hence, the balance additional depreciation of 10% (i.e. 50% of 20%) can be claimed in the immediately succeeding previous year i.e., P.Y. 2016-17

(ii) The statement is not correct.

If an undertaking is set up in any notified backward area in the states of Andhra Pradesh or Bihar or Telangana or West Bengal by a company, it shall be eligible to claim deduction under section 32AC as well as under section 32AD, if it fulfills the conditions specified in section 32AC and the conditions specified in section 32AD.

In the given case, a manufacturing company set up in Vaishali i.e., a notified backward area in the State of Bihar, acquires and installs new plant and machinery for ₹ 30 crores in P.Y. 2015-16. Hence, it will be entitled to deduction under section 32AC (since the investment in new plant and machinery exceeds ₹ 25 crores) as well as under section 32AD (since the undertaking is set-up in a notified backward area in the State of Bihar), assuming that it fulfills the other conditions specified thereunder.

(iii) The statement is not correct.

The proviso to section 36(1)(iii) provides that interest paid on capital borrowed for acquisition of an asset (whether capitalized in the books of account or not) for the period upto the date on which such asset was first put to use shall not be allowed as deduction. This is irrespective of whether the acquisition of asset was for extension of existing business or not.

Therefore, interest paid on capital borrowed for acquisition of an asset for the period upto the date on which such asset was first put to use shall be capitalized even if the acquisition is not for the extension of existing business or profession.

6. **In the hands of the seller, Mr. Sitesh**

As per section 50C(1), where the consideration received or accruing as a result of transfer of land or building or both, is less than the value adopted or assessed or assessable by the stamp valuation authority, the value adopted or assessed or assessable by the stamp valuation authority shall be deemed to be the full value of consideration received or accruing as a result of transfer.

Where the assessee appeals against the stamp valuation and the value is reduced in appeal by the appellate authority (Revenue Divisional Officer, in this case), such value will be regarded as the consideration received or accruing as a result of transfer.

In the given problem, land has been held for a period exceeding 36 months and building for a period less than 36 months immediately preceding the date of transfer. So land is a long-term capital asset, while building is a short-term capital asset.

Particulars	₹
Long term capital gain on sale of land	
Consideration received or accruing as a result of transfer of land	25,00,000
Less: Indexed cost of acquisition ₹ 6,19,000 x 1081/711	9,41,124
Long-term capital gain (A)	**15,58,876**
Short-term capital loss on sale of building	
Consideration received or accruing from transfer of building	10,00,000
Less: Cost of acquisition	12,50,000
Short term capital loss (B)	**(2,50,000)**

As per section 70, short-term capital loss can be set-off against long-term capital gains. Therefore, the net taxable long-term capital gains would be ₹ 13,08,876 (i.e., ₹ 15,58,876 – ₹ 2,50,000). The same would be taxable @ 20% under section 112, after adjusting un-exhausted basic exemption limit, if any, against such long term capital gain.

In the hands of the buyer Mr. Gautam

As per section 56(2)(vii), where an individual or HUF receives from a non-relative, any immovable property for a consideration which is less than the stamp value (or the value reduced by the appellate authority, as in this case) by an amount exceeding ₹ 50,000, then the difference between such value and actual consideration of such property is chargeable to tax as income from other sources. Therefore, ₹ 5,00,000 (i.e. ₹ 35,00,000 - ₹ 30,00,000) would be charged to tax as income from other sources under section 56(2)(vii) in the hands of Mr. Gautam.

7. Section 64(1)(iv) of the Income-tax Act, 1961 provides for the clubbing of income in the hands of the individual, if the income earned is from the assets (other than house property) transferred directly or indirectly to the spouse of the individual, otherwise than for adequate consideration or in connection with an agreement to live apart.

In this case, Mr. Chauhan received a gift of ₹ 4,00,000 on 1.4.2015 from his wife Mrs. Aparna, which he invested in his business immediately. The income to be clubbed in the hands of Mrs. Aparna for the A.Y. 2016-17 is computed as under:

Particulars	Mr. Chauhan's capital contribution (₹)	Capital contribution out of gift from Mrs. Aparna (₹)	Total (₹)
Capital as on 1.4.2015	6,00,000 (10,00,000 – 4,00,000)	4,00,000	10,00,000
Profit for P.Y.2015-16 to be apportioned on the basis of	3,00,000	2,00,000	5,00,000

capital employed on the first day of the previous year i.e. as on 1.4.2015 (3:2)	$\left(5,00,000 \times \frac{3}{5}\right)$	$\left(5,00,000 \times \frac{2}{5}\right)$	

Therefore, the income to be clubbed in the hands of Mrs. Aparna for the A.Y.2016-17 is ₹ 2,00,000.

In case Mrs. Aparna gave the said amount of ₹ 4,00,000 as a *bona fide* loan, then, clubbing provisions would not be attracted.

8. **Computation of Gross Total Income of Mr. Jain for the A.Y. 2016-17**

Particulars	₹	₹
(i) **Income from salary**	70,000	
Less: Loss from house property (set-off as per section 71)	25,000	45,000
(ii) **Capital gains**		
Long term capital gain on sale of land	82,700	
Less: Set-off of business loss as per section 71	40,000	
	42,700	
Less: Set-off of brought forward short term capital loss [Short-term capital loss can be set-off against both short- term capital gains and long-term capital gains as per section 74(1)]	9,700	
	33,000	
Less: Unabsorbed depreciation (can be set-off against any head of income other than salaries)	20,000	13,000
Gross total income		**58,000**

Losses to be carried forward to A.Y.2017-18

	Particulars	₹
(1)	**Loss from speculative business [to be carried forward as per section 73]** [Loss from a speculative business can be set off only against income from another speculative business. Since there is no income from speculative business in the current year, the entire loss of ₹ 22,000 brought forward from A.Y.2015-16 has to be carried forward to A.Y. 2017-18 for set-off against speculative business income of that year. It may be noted that speculative business loss can be carried forward for a maximum of four years as per section 73(4), i.e., upto A.Y.2019-20]	22,000

(2)	**Loss on maintenance of race horses [to be carried forward as per section 74A]** [As per section 74A(3), the loss incurred in the activity of owning and maintaining race horses in any assessment year cannot be set-off against income from any other source other than the activity of owning and maintaining race horses. Such loss can be carried forward for a maximum of four assessment years i.e., upto A.Y.2020-21]	21,000
(3)	**Loss from gambling can neither be set-off nor be carried forward.**	

Notes:

(1) Section 71 permits set-off of losses incurred under one head against income earned under any other head of income. Therefore, loss from house property has been set-off against salary income.

(2) However, there are certain exceptions contained in section 71 on inter-head set-off of losses. Business loss and unabsorbed depreciation cannot be set-off against salary income as per section 71(2A). However, there is no bar in setting-off the business loss and unabsorbed depreciation against long term capital gain. Hence, business loss and unabsorbed depreciation have been set off against long term capital gain.

9. (i) Deduction available to Mr. Hariharan under Chapter VI-A for A.Y.2016-17

Section	Particulars	₹	₹
80C	Deposit in public provident fund ₹ 1,60,000 (deduction restricted to ₹ 1,50,000)	1,50,000	
	Life insurance premium paid ₹ 25,000 (deduction restricted to ₹ 20,000, being 20% of ₹ 1,00,000, which is the sum assured, since the policy was taken before 01.04.2012)	20,000	
	Five year term deposit with bank	50,000	
		2,20,000	
	Restricted to		1,50,000
80CCD(1)	Contribution to NPS of the Central Government, ₹ 1,60,000 [₹ 2,10,000 – ₹ 50,000, being deduction under section 80CCD(1B)], restricted to 10% of salary [₹ 2,10,000 x 10/15] **[See Note 1]**		1,40,000
			2,90,000

80CCE	Aggregate deduction under section 80C and 80CCD(1), ₹ 2,90,000, but restricted to		1,50,000
80CCD(1B)	₹ 50,000 would be eligible for deduction in respect of contribution to NPS of the Central Government		50,000
80CCD(2)	Employer contribution to NPS, restricted to 10% of salary **[See Note 2]**		1,40,000
80D	(i) (a) Medical insurance premium for self	22,000	
	(b) Preventive health check up ₹ 5,000 for wife restricted to ₹ 3,000 (₹ 25,000 - ₹ 22,000, since maximum allowable deduction is ₹ 25,000)	3,000	
		25,000	
	(ii) (a) Health Insurance premium for his father	26,000	
	(b) Preventive health check up ₹ 5,000 restricted to ₹ 2,000 (₹ 5,000 - ₹ 3,000), since maximum allowable deduction in respect of preventive health check up under section 80D is ₹ 5,000[1].	2,000	
		28,000	
	Whole of the amount of ₹ 28,000 allowed as deduction, since maximum allowable deduction is ₹ 30,000, where the parent is a senior citizen.		
	Total of (i) and (ii)		**53,000**
80DD	Deduction of ₹ 1,25,000 in respect of expenditure on medical treatment of his mother, being a person with severe disability would be allowed irrespective of the fact that amount of expenditure incurred is ₹ 50,000		1,25,000
Deduction under Chapter VI-A			**5,18,000**

[1] In the alternative, preventive health check-up of ₹ 4,000 of his father can be claimed, in which case, expenses on preventive health check-up of wife can be claimed only to the extent of ₹ 1,000. In such case also, the total deduction under section 80D would be ₹ 53,000 (₹ 23,000 + ₹ 30,000)

Notes:

(1) The deduction under section 80CCD(1B) would not be subject to overall limit of ₹ 1.50 lakh under section 80CCE. Therefore, it is more beneficial for Mr. Hariharan to claim deduction under section 80CCD(1B) first in respect of contribution to NPS. Thereafter, the remaining amount of ₹ 1,60,000 can be claimed as deduction under section 80CCD(1), subject to a maximum limit of 10% of salary i.e. ₹ 1,40,000.

(2) The entire employer's contribution to notified pension scheme has to be first included under the head "Salaries" while computing gross total income and thereafter, deduction under section 80CCD(2) would be allowed, subject to a maximum of 10% of salary. Deduction under section 80CCD(2) is also not subject to the overall limit of ₹ 1,50,000 under section 80CCE

(ii) If the contribution towards NPS is ₹ 1,40,000, here again, it is beneficial for Mr. Hariharan to first claim deduction of ₹ 50,000 under section 80CCD(1B) and the balance of ₹ 90,000 can be claimed under section 80CCD(1), since the deduction available under section 80CCD(1B) is over and above the aggregate limit of ₹ 1,50,000 under section 80CCE. In any case, the aggregate deduction of ₹ 2,40,000 [i.e., ₹ 1,50,000 under section 80C and ₹ 90,000 under section 80CCD(1)] cannot exceed the overall limit of ₹ 1,50,000 under section 80CCE. The total deduction under Chapter VIA would remain the same i.e., ₹ 5,18,000.

10. Computation of total income and tax liability of Dr. Ashish Puri for the A.Y.2016-17

Particulars	₹
Income from salary (Working Note – 1)	96,000
Income from business (Working Note – 2)	2,57,050
Long-term capital gains (Working Note – 3)	2,88,432
Income from other sources (Working Note – 4)	60,000
Gross Total Income	**7,01,482**
Less: Deduction under Chapter VI-A (Working Note – 5)	1,55,000
Total Income	**5,46,482**
Tax on total income (Working Note - 6)	63,991
Add: Education cess @ 2% and SHEC @1%	1,920
Total tax liability	65,911
Less: Tax deducted at source (TDS)	12,000
Tax payable	**53,911**
Rounded off	**53,910**

Working Notes:

1. **Computation of salary income**

Particulars	₹
Gross Salary (₹ 8,000×12)	96,000
Less: Deduction under section 16	Nil
Net Salary	**96,000**

2. **Computation of income under the head "Profits and gains of business or profession"**

Particulars	₹	₹
Net Income as per Income and Expenditure Account		2,51,800
Add: Expenses disallowed:		
Depreciation (₹ 91,000 – ₹ 50,000)	41,000	
Cost of medicine for self-use	25,000	
Donation to Prime Minister's National Relief Fund	5,000	71,000
		3,22,800
Less: Dividend from Indian companies	15,000	
Income-tax refund	2,750	
Winning from Lotteries	28,000	
Honorarium for valuing answer books	20,000	65,750
		2,57,050

3. **Computation of Capital Gains**

Particulars	₹	₹
Sale consideration	12,00,000	
Valuation as per Stamp Valuation Authority	14,00,000	
(Value to be taken is the higher of actual sale consideration or valuation adopted for stamp duty purposes as per section 50C)		
Consideration for the purpose of capital gain		**14,00,000**
Less: Cost of acquisition = ₹ 4,00,000 x 1081/389		11,11,568
Long term capital gain		**2,88,432**

4. **Computation of income under the head "Income from other sources"**

Particulars	₹	₹
Dividend from Indian Companies [Exempt u/s 10(34)]		-
Honorarium for valuing answer books		20,000

Winning from Lotteries (Net)	28,000	
Add: TDS	12,000	40,000
Income from other sources		**60,000**

Note: As per section 58(4), no expense or deduction is allowable in respect of winnings from lotteries.

5. **Computation of deduction under Chapter VI-A**

Particulars	₹
U/s 80C Life Insurance Premium (whole amount is allowed as deduction since it is within the limit of 10% of sum assured)	45,000
PPF	1,50,000
	1,95,000
Restricted to	1,50,000
U/s 80G Donation to Prime Minister's National Relief Fund [See Note below]	5,000
Total deduction under Chapter VI-A	**1,55,000**

Note –The donation made to the Prime Minister's National Relief Fund qualifies for 100% deduction under section 80G.

6. **Computation of tax on total income**

Particulars	₹
Tax on agricultural income plus non-agricultural income i.e. tax on ₹ 8,21,482 (being ₹ 2,75,000 + ₹ 5,46,482) [See Note below]	93,991
Less: Tax on agricultural income plus basic exemption limit i.e. tax on ₹ 5,25,000, (being ₹ 2,75,000 + ₹ 2,50,000)	30,000
Tax on total income	**63,991**

Note: Tax on ₹ 5,46,482 plus agricultural income of ₹ 2,75,000 is computed hereunder:

Particulars	₹
Tax on long term capital gain	
₹ 2,88,432 @ 20%	57,686
Tax on winnings from lotteries	
₹ 40,000 @ 30%	12,000

Tax on balance income of ₹ 4,93,050 (₹ 8,21,482 – ₹ 2,88,432 – ₹ 40,000)	24,305
	93,991

Note: Agricultural income is exempt from tax. It is considered for rate purpose only.

7. Any sum received under a life insurance policy is wholly exempt from tax under section 10(10D), subject to satisfaction of conditions given thereunder. In this case, it is presumed that all the conditions are satisfied.

11. (i) Theta Co-operative Bank has to deduct tax at source@10% on the interest of ₹ 48,000 (8% × ₹ 12 lakh × ½) under section 194A.

(ii) Since Omega Bank has adopted CBS, the aggregate interest credited/paid by all branches has to be considered, and if the same exceeds ₹ 10,000, tax is deductible under section 194A. Omega Bank has to deduct tax at source @10% under section 194A, since the aggregate interest on fixed deposit with the three branches of the bank is ₹ 16,000, which exceeds the threshold limit of ₹ 10,000.

Branch	Amount of deposit (₹)	Rate of Interest	Period in months	Amount of Interest (₹)
Adyar	60,000	10%	10	5,000
Anna Nagar	80,000	10%	9	6,000
Nungambakkam	75,000	10%	8	5,000
Total				**16,000**

(iii) Tax has to be deducted @ 10% under section 194A by Gamma Bank on the interest of ₹ 13,000 (See Working Note below) falling due on recurring deposit on 31.3.2016 to Ms. Meena, since –

(1) "recurring deposit" has been included in the definition of "time deposit"; and

(2) such interest exceeds the threshold limit of ₹ 10,000.

Working Note:

Computation of Interest

= ₹ 20,000 x 10% x [(12+11+10+9+8+7+6+5+4+3+2+1)/12]

= ₹ 2,000 x (78/12)

= ₹ 13,000

12. Any person who has furnished a return under section 139(1) or in pursuance of a notice issued under section 142(1) can file a revised return if he discovers any omission or any wrong statement in the return filed earlier. Accordingly,

(i) A belated return filed under section 139(4) cannot be revised. Only a return furnished under section 139(1) or in pursuance of a notice issued under section 142(1) can be revised.

(ii) A return revised earlier can be revised again as the first revised return replaces the original return. Therefore, if the assessee discovers any omission or wrong statement in such a revised return, he can furnish a second revised return within the prescribed time i.e. within one year from the end of the relevant assessment year or before the completion of assessment, whichever is earlier.

(iii) A return of loss filed under section 139(3) is deemed to be return filed under section 139(1), and therefore, can be revised under section 139(5).

13. Computation of assessable value and excise duty payable

Particulars	**(₹)**
Price of machine excluding taxes and duties	10,00,000
Add: Outward handling charges [Note 1]	-
Protective packing charges [Note 2]	12,500
Installation and erection expenses [Note 3]	-
Testing and inspection charges [Note 2]	40,000
Delayed payment charges [Note 4]	-
Dharmada charged in the invoice [Note 5]	10,000
Assessable value	10,62,500
Excise duty payable @ 12.5% [rounded off]	**1,32,813**

Notes:

1. Outward handling charges are not included in the assessable value as the same are incurred after the place of removal.
2. Protective packing charges and testing and inspection charges have been included in the assessable value as such payments are 'in connection with sale'.
3. Installation and erection expenses have not been included in the assessable value as the same are incurred after the place of removal and after the installation and erection, machine has been permanently affixed to earth and thus, it has resulted in an immovable property.
4. Delayed payment charges are not includible as the same are finance charges and cannot be considered as payment by reason of sale.
5. Dharmada charged in the invoice and recovered from the customer is includible in the assessable value.

14. Computation of customs duty payable

Particulars	**Rate %**	**Amount (₹)**	**Amount of Duty (₹)**
Assessable value		2,00,000	
Basic customs duty	10	20,000	20,000
Sub-total for calculating CVD		2,20,000	
CVD (₹ 2,20,000 x excise duty rate)	12.5	27,500	27,500
Sub-total for education cess on customs (₹ 20,000 + ₹ 27,500)		47,500	
Education cess of customs	2	950	950
Secondary and Higher Education cess of customs	1	475	475
Sub-total for special CVD (₹ 2,00,000 + ₹ 20,000 + ₹ 27,500 + ₹ 950 + ₹ 475)		2,48,925	
Special CVD u/s 3(5)	4	9,957	9,957
Total customs duty payable			**58,882**

Since ABC Ltd. is a service provider, it can avail CENVAT credit of only CVD i.e. only of ₹ 27,500 and not of special CVD.

15. (i) Since in the given case, sale is effected by transfer of documents of title to the goods after the goods have crossed the customs frontiers of India, it is not an inter-State sale, but a sale in the course of export.

(ii) The sale is completed at Delhi itself. Therefore, the sale does not occasion the movement of goods from one State to another. Hence, sale of goods by N to M is not an inter-State sale.

(iii) Since in this case, the sale has occasioned the import of the goods into the territory of India, it is not an inter-State sale, but a sale in the course of import.

16. Computation of total sales value

Particulars	₹
Intra-State purchases of raw material [excluding VAT of ₹ 10,000 (80,000 x 12.5%)]	80,000
High seas purchases of raw materials [Note 1]	2,03,500
Purchase of raw materials from West Bengal [Note 2]	51,000
Transportation charges, wages and manufacturing expenses	3,50,000
Cost of production	6,84,500

Add: Profit margin 10%	68,450
Sale price (exclusive of VAT)	7,52,950
Add: VAT @ 12.5% (rounded off)	94,119
Total sales value (invoice value)	**8,47,069**

Computation of net VAT liability

	₹
VAT paid on sales @ 12.5%	94,119
Less: Input tax credit on intra-State purchases [Note 3]	10,000
Net VAT payable	**84,119**

Notes:

1. Duty paid on high seas purchases i.e., imports is not a State VAT, so input tax credit is not available in respect of the same and it is a part of cost of production.
2. Input tax credit in respect of tax paid on inter-State purchases is not allowed and it is a part of cost of production.
3. Tax on intra-State purchases is ₹ 10,000. As credit of the same will be available, it is not included in the cost of production.
4. Interest on loan has been excluded while calculating the cost of production as the loan is availed for purposes other than working capital.

17. **(a)** Earlier, services by way of carrying out any process amounting to manufacture or production of goods were covered in the Negative List of services under section 66D of the Finance Act, 1994.

However, Finance Act, 2015 has amended section 66D to exclude process for production or manufacture of alcoholic liquor for human consumption from the ambit of negative list. Further, the definition of the term "process amounting to manufacture or production of goods" as provided in section 65B has also been amended to exclude from its scope, the process amounting to manufacture of "alcoholic liquors for human consumption". Simultaneously, Mega Exemption *Notification No. 25/2012 ST dated 20.06.2012* has been amended to withdraw exemption pertaining to intermediate production of alcoholic liquor for human consumption.

Consequently, service tax would be leviable on manufacture of alcoholic liquor for human consumption on job-work basis by AB Pvt. Ltd.

(b) Earlier, "admission to entertainment events or access to amusement facilities" was covered in the Negative List of services under section 66D of the Finance Act, 1994.

However, the said entry has been omitted from section 66D vide the Finance Act, 2015. Therefore, service tax would be leviable on admission to entertainment event or access to amusement facility.

Thus, entry fee to Splash and Splutter water park (being an entry to amusement facility) will be chargeable to service tax.

18. In case of “associated enterprises”, where the person providing the service is located outside India, the point of taxation shall be:-

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

or

(b) date of making the payment

whichever is earlier.

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

(a) the date of debit in the books of account of SIL i.e., 05.08.2015

or

(b) date of making the payment i.e., 24.09.2015

Thus, the point of taxation will be 05.08.2015.

19. Computation of service tax liability of BIE Academy for the month of July, 2015

Particulars	**₹**
Free online access for coaching (Note 1)	Nil
Advance fees collected from students for online coaching sessions (Note 2)	12,00,000
Advance received from ABC School (Note 2 & 3)	5,92,000
Value of taxable services including service tax	17,92,000
Service tax liability $\left(\frac{17,92,000 \times 14}{114}\right)$ **(rounded off)**	**2,20,070**

Notes:

1. Service is an activity carried out, *inter alia,* for a consideration. Therefore, since no consideration is involved in case of free services, service tax is not payable thereon.
2. Since, services agreed to be provided are also chargeable to service tax, advance received will be liable to service tax [Section 66B].

   Advanced received is taxable at the time when such advance is received [Rule 3 of the Point of Taxation Rules, 2011].

3. Since service becomes taxable on an agreement to provide a service, deposits forfeited (on cancellation of agreement) would represent consideration for the agreement that was entered into for provision of service. Further, had the advance deposit alongwith service tax been returned to ABC School on cancellation of agreement, credit of such service tax would have been available.

4. Since the service tax paid in preceding financial year 2014-15 is ₹ 15.6 lakh, the aggregate value of taxable services must have exceeded ₹ 10 lakh in said financial year. Thus, BIE Academy is not eligible for small service provider exemption in the current financial year 2015-16.

20. **Computation of service tax payable**

S. No.	Particulars	Value of taxable services (₹)	Service tax liability (₹)
1.	Services by way of waxing of apples to provide it an artificial sheen for increasing its marketability [Note 1]	Nil	
2.	Admission to a Railway Museum [Note 2]	Nil	
3.	Transportation of patients to ABC Nursing Home and Bheem Multispecialty Hospital, in an ambulance owned by XYZ Ltd. [Note 3]	Nil	
4.	Admission to a Telly Award Function [Note 4]	5,10,000	5,10,000 ×14% = 71,400
5.	Transportation of milk by a goods transport agency [Note 5]	Nil	

Notes:

As per mega exemption *Notification No. 25/2012 ST dated 20.06.2012:*

1. services by way of waxing of fruits which do not change/alter the essential characteristics of the said fruits are exempt from service tax.
2. services provided by way of admission to a museum are exempt from service tax.
3. ambulance services provided by an entity which is not a clinical establishment or an authorised medical practitioner or paramedics are also exempt from service tax.
4. service by way of admission to award functions is exempt from service tax if the amount charged is upto ₹ 500 per person for right to admission to such event. In case the amount charged per person exceeds ₹ 500, entire consideration would be liable to service tax.

5. services of transportation of milk, salt and food grain including flours, pulses and rice by a goods carriage are exempt from service tax.

21. Mega exemption *Notification No. 25/2012 ST dated 20.06.2012* exempts services by an artist by way of a performance in folk or classical art forms of (i) music, or (ii) dance, or (iii) theatre, if the consideration charged for such performance is not more than ₹ 1,00,000. However, exemption will not apply to service provided by such artist as a brand ambassador.

In view of the aforesaid provisions, services provided by Kesar Maharaj are exempt from service tax as consideration for the classical dance performance has not exceeded ₹ 1,00,000. Therefore, his service tax liability is nil.

(i) If the consideration charged for the said performance by Kesar Maharaj is ₹ 1,20,000, he will be liable to pay service tax on the same as although the performance is by way of classical art form of dance, consideration charged for such performance has exceeded ₹ 1,00,000. His service tax liability would, therefore, be ₹ 16,800 (₹ 1,20,000 × 14%).

(ii) If Kesar Maharaj is a brand ambassador of a food product and aforesaid performance is for the promotion of such food product, he will be liable to pay service tax as aforesaid exemption is not applicable to service provided by an artist as a brand ambassador. His service tax liability would, therefore, be ₹ 13,790 (₹ 98,500 × 14%).

(iii) If Kesar Maharaj gives a contemporary Bollywood style dance performance, such performance will not be eligible for aforesaid exemption. The reason for the same is that although the consideration charged does not exceed ₹ 1,00,000, said performance is not in folk or classical art forms of dance. Hence, service tax would be payable on the same. His service tax liability would, therefore, be ₹ 13,790 (₹ 98,500 × 14%).

22. Person liable for paying the service tax in relation to the services of booking of tickets for travel by air provided by an air travel agent, has an option to pay following amounts instead of paying service tax at the rate of 14%:-

In the case of	**Option to pay an amount calculated at the rate of**
Domestic bookings of passage for travel by air	0.7% of the basic fare
International bookings of passage for travel by air	1.4% of the basic fare

Here, basic fare means that part of the air fare on which commission is normally paid to the air travel agent by the airline.

Therefore, Mr. Paritosh can pay service tax at the above-mentioned alternative rates instead of paying service tax at 14%. However, he should keep in mind that if he exercises such an option, the same will apply uniformly in respect of all the bookings of passage for travel by air made by him and cannot be changed during a financial year under any circumstances.

Yes, the option of payment of service tax at alternative rates is available in respect of three other services namely, life insurance service, purchase or sale of foreign currency including money changing and promotion, marketing or organising/assisting in organising lottery.

23. The statement is partially correct.

A manufacturer can take CENVAT credit of the excise duty paid on the inputs when the same are received in-

- the factory of the manufacturer; or
- the premises of job worker, in case goods are sent directly to the job worker on the direction of the manufacturer.

An output service provider can take CENVAT credit of the excise duty paid on the inputs when the same are-

- received in the premises of the provider of output service, or
- received in the premises of job worker, in case goods are sent directly to the job worker on the direction of the output service provider; or
- delivered to such provider (at a place other than his premises), subject to maintenance of documentary evidence of delivery and location of the inputs.

24. **Computation of CENVAT credit available with LT Pvt. Ltd.**

Particulars	₹
Machine for manufacture of rubber soles [Note 1]	5,00,000
Rubber sheets for manufacture of slippers [Note 2]	5,00,000
Adhesives [Note 2]	50,000
Club membership fee of employees [Note 3]	Nil
Expenses incurred on advertising the slippers on television [Note 4]	5,00,000
Total CENVAT credit available	**15,50,000**

Notes:

1. Since LT Pvt. Ltd. is not a SSI unit, CENVAT credit of only upto 50% of the excise duty paid is available in respect of the eligible capital goods, in the year of purchase [Rule 4 of CCR].
2. Raw material (rubber sheets) and consumables (adhesives) are eligible inputs.
3. Services used primarily for personal use or consumption of any employee are excluded from the definition of input service.
4. Advertising service is an eligible input service.