

## PAPER – 1: ACCOUNTING

### PART – I: ANNOUNCEMENTS STATING APPLICABILITY & NON-APPLICABILITY FOR MAY, 2018 EXAMINATION

#### A. Applicable for May, 2018 examination

##### I. Companies Act, 2013

Relevant Sections of the Companies Act, 2013 notified up to 31<sup>st</sup> October, 2017 will be applicable for May, 2018 Examination.

##### II. Notification dated 13th June, 2017 to exempt startup private companies from preparation of Cash Flow Statement as per Section 462 of the Companies Act 2013

As per the Amendment, under Chapter I, clause (40) of section 2, new exemption has been provided to a startup private company besides one person company, small company and dormant company. Accordingly, a startup private company is not required to include the cash flow statement in the financial statements.

Thus the financial statements, with respect to one person company, small company, dormant company and private company (if such a private company is a start-up), may not include the cash flow statement.

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

Amendments made by MCA on 30.3.2016 in the Companies (Accounting Standards) Rules, 2006 have been made applicable for May, 2018 examination.

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

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

Name of the standard	Para no.	As per the Companies (Accounting Standards) Rules, 2006	As per the Companies (Accounting Standards) Amendment Rules, 2016	Implication
AS 2	4 (an extract)	Inventories do not include machinery	Inventories do not include spare	Now, inventories also do not

		spares which can be used only in connection with an item of fixed asset and whose use is expected to be irregular; such machinery spares are accounted for in accordance with Accounting Standard (AS) 10, Accounting for Fixed Assets.	parts, servicing equipment and standby equipment which meet the definition of property, plant and equipment as per AS 10, Property, Plant and Equipment. Such items are accounted for in accordance with Accounting Standard (AS) 10, Property, Plant and Equipment.	include servicing equipment and standby equipment other than spare parts if they meet the definition of property, plant and equipment as per AS 10, Property, Plant and Equipment.
	27	Common classifications of inventories are raw materials and components, work in progress, finished goods, stores and spares, and loose tools.	Common classifications of inventories are: (a) Raw materials and components (b) Work-in-progress (c) Finished goods (d) Stock-in-trade (in respect of goods acquired for trading) (e) Stores and spares (f) Loose tools (g) Others (specify nature)".	Para 27 of AS 2 requires disclosure of inventories under different classifications. One residual category has been added to the said paragraph i.e. 'Others'.

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

			investment property.	
	30	An enterprise holding investment properties should account for them as long term investments.	An enterprise holding investment properties should account for them in accordance with cost model as prescribed in AS 10, Property, Plant and Equipment.	Accounting of investment property shall now be in accordance with AS 10 i.e. at cost model
AS 14	3(a)	Amalgamation means an amalgamation pursuant to the provisions of the Companies Act, 1956 or any other statute which may be applicable to companies.	Amalgamation means an amalgamation pursuant to the provisions of the Companies Act, 2013 or any other statute which may be applicable to companies and includes 'merger'.	Definition of Amalgamation has been made broader by specifically including 'merger'.
	18 and 39	In such cases the statutory reserves are recorded in the financial statements of the transferee company by a corresponding debit to a suitable account head (e.g., 'Amalgamation Adjustment Account') which is disclosed as a part of 'miscellaneous expenditure' or other similar category in the balance sheet. When the identity of the statutory reserves is no longer required to be maintained, both the reserves and the	In such cases the statutory reserves are recorded in the financial statements of the transferee company by a corresponding debit to a suitable account head (e.g., 'Amalgamation Adjustment Reserve') which is presented as a separate line item. When the identity of the statutory reserves is no	Corresponding debit on account of statutory reserve in case of amalgamation in the nature of purchase is termed as 'Amalgamation Adjustment Reserve' and is now to be presented as a separate line item since there is not sub-heading like 'miscellaneous expenditure' in Schedule III to the

		aforesaid account are reversed.	longer required to be maintained, both the reserves and the aforesaid account are reversed.	Companies Act, 2013
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**B. Not applicable for May, 2018 examination****Non-Applicability of Ind ASs for May, 2018 Examination**

The Ministry of Corporate Affairs has notified Companies (Indian Accounting Standards) Rules, 2015 on 16<sup>th</sup> February, 2015, for compliance by certain class of companies. These Ind AS have not been made applicable for May, 2018 Examination.

**PART – II: QUESTIONS AND ANSWERS****QUESTIONS****Financial Statements of Companies**

1. Kapil Ltd. has authorized capital of ₹ 50 lakhs divided into 5,00,000 equity shares of ₹ 10 each. Their books show the following balances as on 31<sup>st</sup> March, 2017:

	₹		₹
Inventory 1.4.2016	6,65,000	Bank Current Account	20,000
Discounts & Rebates allowed	30,000	Cash in hand	8,000
Carriage Inwards	57,500	Interest (bank overdraft)	1,11,000
Patterns	3,75,000	Calls in Arrear @ ₹2 per share	10,000
Rate, Taxes and Insurance	55,000	Equity share capital	20,00,000
Furniture & Fixtures	1,50,000	(2,00,000 shares of ₹ 10 each)	
Purchases	12,32,500	Bank Overdraft	12,67,000
Wages	13,68,000		
Freehold Land	16,25,000	Trade Payables (for goods)	2,40,500
Plant & Machinery	7,50,000	Sales	36,17,000
Engineering Tools	1,50,000	Rent (Cr.)	30,000
Trade Receivables	4,00,500	Transfer fees received	6,500

Advertisement	15,000	Profit & Loss A/c (Cr.)	67,000
Commission & Brokerage	67,500	Repairs to Building	56,500
Business Expenses	56,000	Bad debts	25,500

The inventory (valued at cost or market value, which is lower) as on 31<sup>st</sup> March, 2017 was ₹ 7,08,000. Outstanding liabilities for wages ₹ 25,000 and business expenses ₹ 36,000. Dividend declared @ 12% on paid-up capital and it was decided to transfer to reserve @ 2.5% of profits.

Charge depreciation on closing written down amount of Plant & Machinery @ 5%, Engineering Tools @ 20%; Patterns @ 10%; and Furniture & Fixtures @ 10%. Provide 25,000 as doubtful debts after writing off ₹ 16,000 as bad debts. Provide for income tax @ 30%. Corporate Dividend Tax Rate @ 17.304 (wherein Base Rate is 15%).

You are required to prepare Statement of Profit & Loss for the year ended 31<sup>st</sup> March, 2017 and Balance Sheet as on that date.

#### Cash flow statement

2. On the basis of the following information prepare a Cash Flow Statement for the year ended 31<sup>st</sup> March, 2017 (Using direct method):
  - (i) Total sales for the year were ₹ 398 crores out of which cash sales amounted to ₹ 262 crores.
  - (ii) Receipts from credit customers during the year, totalled ₹ 134 crores.
  - (iii) Purchases for the year amounted to ₹ 220 crores out of which credit purchase was 80%.
 

Balance in creditors as on

1.4.2016	₹ 84 crores
31.3.2017	₹ 92 crores
  - (iv) Suppliers of other consumables and services were paid ₹ 19 crores in cash.
  - (v) Employees of the enterprises were paid 20 crores in cash.
  - (vi) Fully paid preference shares of the face value of ₹ 32 crores were redeemed. Equity shares of the face value of ₹ 20 crores were allotted as fully paid up at premium of 20%.
  - (vii) Debentures of ₹ 20 crores at a premium of 10% were redeemed. Debenture holders were issued equity shares in lieu of their debentures.
  - (viii) ₹ 26 crores were paid by way of income tax.

- (ix) A new machinery costing ₹ 25 crores was purchased in part exchange of an old machinery. The book value of the old machinery was ₹ 13 crores. Through the negotiations, the vendor agreed to take over the old machinery at a higher value of ₹ 15 crores. The balance was paid in cash to the vendor.
- (x) Investment costing ₹ 18 cores were sold at a loss of ₹ 2 crores.
- (xi) Dividends totalling ₹ 15 crores (including dividend distribution tax of ₹ 2.7 crores) was also paid.
- (xii) Debenture interest amounting ₹ 2 crore was paid.
- (xiii) On 31<sup>st</sup> March 2016, Balance with Bank and Cash on hand totalled ₹ 2 crores.

#### Profit/Loss prior to Incorporation

3. The Business carried on by Kamal under the name "K" was taken over as a running business with effect from 1<sup>st</sup> April, 2016 by Sanjana Ltd., which was incorporated on 1<sup>st</sup> July, 2016. The same set of books was continued since there was no change in the type of business and the following particulars of profits for the year ended 31<sup>st</sup> March, 2017 were available.

	₹	₹
Sales: Company period	40,000	
Prior period	<u>10,000</u>	50,000
Selling Expenses	3,500	
Preliminary Expenses written off	1,200	
Salaries	3,600	
Directors' Fees	1,200	
Interest on Capital (Upto 30.6.2016)	700	
Depreciation	2,800	
Rent	4,800	
Purchases	25,000	
Carriage Inwards	<u>1,019</u>	<u>43,819</u>
Net Profit		<u>6,181</u>

The purchase price (including carriage inwards) for the post-incorporation period had increased by 10 percent as compared to pre-incorporation period. No stocks were carried either at the beginning or at the end.

You are required to draw up a statement showing the amount of pre and post in corporation period profits stating the basis of allocation of expenses.

**Accounting for Bonus Issue**

4. Following is the extract of the Balance Sheet of Manoj Ltd. as at 31<sup>st</sup> March, 20X1

	₹
<b>Authorised capital:</b>	
30,000 12% Preference shares of ₹ 10 each	3,00,000
4,00,000 Equity shares of ₹ 10 each	<u>40,00,000</u>
	<u>43,00,000</u>
<b>Issued and Subscribed capital:</b>	
24,000 12% Preference shares of ₹ 10 each fully paid	2,40,000
2,70,000 Equity shares of ₹ 10 each, ₹ 8 paid up	21,60,000
<b>Reserves and surplus:</b>	
General Reserve	3,60,000
Capital Redemption Reserve	1,20,000
Securities premium (collected in cash)	75,000
Profit and Loss Account	6,00,000

On 1<sup>st</sup> April, 20X1, the Company has made final call @ ₹ 2 each on 2,70,000 equity shares. The call money was received by 20<sup>th</sup> April, 20X1. Thereafter, the company decided to capitalize its reserves by way of bonus at the rate of one share for every four shares held.

Show necessary journal entries in the books of the company and prepare the relevant extract of the balance sheet as on 30<sup>th</sup> April, 20X1 after bonus issue.

**Internal Reconstruction of a Company**

5. Proficient Infosoft Ltd. is in the hands of a Receiver for Debenture Holders who holds a charge on all asset except uncalled capital. The following statement shows the position of the company as on 30<sup>th</sup> June, 2016:

Liabilities	₹	Assets	₹
8,000 shares of ₹ 100 each	4,80,000	Property	10,80,000
₹ 60 paid up		Plant & Machinery	4,36,000
First Debentures	3,60,000	Cash in hand	<u>3,24,000</u>
Second Debentures	7,80,000		18,40,000
Unsecured trade payables	<u>5,40,000</u>	Uncalled capital	<u>3,20,000</u>
	<u>21,60,000</u>		<u>21,60,000</u>



A holds the first debentures for ₹ 3,60,000 and second debentures for ₹ 3,60,000. He is also an unsecured trade payable for ₹ 1,08,000. B holds second debentures for ₹ 3,60,000 and is an unsecured trade payable for ₹ 72,000.

The following scheme of reconstruction is proposed:

- (i) A is to cancel ₹ 2,52,000 of the total debt owing to him; to bring ₹ 36,000 in cash and to take first debentures (in cancellation of those already issued to him) for ₹ 6,12,000 in satisfaction of all his claims.
- (ii) B to accept ₹ 1,08,000 in cash in satisfaction of all claims by him.
- (iii) In full settlement of 60% of the claim, unsecured trade payable (other than A and B) agreed to accept three shares of ₹ 25 each, fully paid against their claim for each ₹ 100.

The balance of 40% is to be postponed and to be payable at the end of three years from the date of Court's approval of the scheme. The nominal share capital is to be increased accordingly.

- (iv) Uncalled capital is to be called up in full and ₹ 75 per share cancelled, thus making the shares of ₹ 25 each.

Assuming that the scheme is duly approved by all parties interested and by the Court, give necessary journal entries.

### Amalgamation of Companies

6. Given below are the summarized Balance Sheet of two companies as on 31<sup>st</sup> March, 2017.

#### A Limited

Liabilities	₹	Assets	₹
Share Capital:		Patent	1,00,000
<u>Issued and fully paid up</u>		Building	5,40,000
50,000 8% Cumulative		Plant and Machinery	15,10,000
Preference Shares of ₹ 10 each	5,00,000	Furniture	75,000
1,50,000 Equity shares of ₹ 10 each	15,00,000	Investment	1,55,000
General Reserve	7,65,000	Stock	3,58,000
Profit and Loss account	1,25,000	Sundry Debtors	72,000
Sundry Creditors	<u>60,000</u>	Cash and Bank	<u>1,40,000</u>
	29,50,000		29,50,000

**B Limited**

Liabilities	₹	Assets	₹
Share Capital:		Goodwill	62,000
<u>Issued and fully paid</u>		Motor Car	1,26,000
50,000 Shares of ₹ 10 each	5,00,000	Furniture	58,000
Profit and Loss Account	45,000	Stock	2,40,000
Sundry Creditors	31,000	Sundry Debtors	70,000
		Cash and Bank	<u>20,000</u>
	<u>5,76,000</u>		5,76,000

It has been agreed that both these companies should be wound up and a new company AB Ltd. should be formed to acquire the assets of both the companies on the following terms and conditions:

- (i) AB Ltd. is to have an authorized capital of ₹ 36,00,000 divided into 60,000, 8% cumulative preference shares of ₹ 10 each and 3,00,000 equity shares of ₹ 10 each.
- (ii) AB Ltd. to purchase the whole of the assets of A Ltd. (except cash and Bank balances) for ₹ 28,25,000 to be settled as to ₹ 5,75,000 in cash and as to the balance by issue of 1,80,000 equity shares, credited as fully paid, to be treated as valued at ₹ 12.50 each.
- (iii) AB Ltd. is to purchase the whole of the assets of B Ltd. (except cash and bank balances) for ₹ 4,91,000 to be settled as to ₹ 16,000 in cash and as to the balance by issue of 38,000 equity shares, credited as fully paid, to be treated as valued at ₹ 12.50 each.
- (iv) A Ltd. and B Ltd. both are to be wound up, the two liquidators distributing the shares in AB Ltd. in kind among the equity shareholders of the respective companies.
- (v) The creditors of A Ltd. and B Ltd. are considered to be paid by the liquidators of the respective companies and not taken over by AB Ltd.
- (vi) The liquidator of A Ltd. is to pay the preference shareholders ₹ 12 in cash for every share held in full satisfaction of their claims.
- (vii) AB Ltd. is to make a public issue of 60,000, 8% cumulative preference shares at a premium of 10% and 30,000 equity shares at the issue price of ₹ 12.50 per share, all amount payable in full on application.

It is estimated that the cost of liquidation (including the liquidators' remuneration) will be ₹ 10,000 in case of A Ltd. and ₹ 5,000 in case of B Ltd. and that the preliminary expenses of AB Ltd. will amount to ₹ 24,000 exclusive of the underwriting commission of ₹ 38,900 payable on the public issue.

You are required to prepare the initial Balance Sheet of AB Ltd. on the basis that all assets other than goodwill are taken over at the book value and preliminary expenses and underwriting commission are to be written off.

### Average Due Date

7. A merchant trader having accepted the following several bills falling due on different dates, now desires to have these bills cancelled and to accept a new bill for the whole amount payable on the average due date:

Sl. No.	Date of Bills	Amount (₹)	Usance of the bill
1	1 <sup>st</sup> May, 2017	500	2 months
2	10 <sup>th</sup> May, 2017	300	3 months
3	5 <sup>th</sup> June, 2017	400	2 months
4	25 <sup>th</sup> June, 2017	375	1 month
5	10 <sup>th</sup> July, 2017	500	2 months

You are required to find the said average due date.

Any fraction of a day arising from the calculation to be considered as full day.

### Account Current

8. The following are the transactions that took place between Rohan & Sunil during the half year ended 30<sup>th</sup> June, 2017:

		₹
i	Balance due to Rohan by Sunil on 1 January, 2017	3,010
ii	Goods sold by Rohan to Sunil on 7 January, 2017	4,430
iii	Goods purchased by Rohan from Sunil on 16 February, 2017	6,480
iv	Goods returned by Rohan to Sunil on 18 February, 2017 (out of the purchases of 16 February, 2017)	560
v	Goods sold by Sunil to Rohan on 24 <sup>th</sup> March, 2017	3,560
vi	Bill accepted by Rohan at 3 months on 22 <sup>nd</sup> April, 2017	1,500
vii	Cash paid by Rohan to Sunil on 29 <sup>th</sup> April, 2017	2,500
viii	Goods sold by Rohan to Sunil on 17 <sup>th</sup> May, 2017	2,710
ix	Goods sold by Sunil to Rohan on 22 <sup>nd</sup> June, 2017	2,280

Draw up an account current to be rendered by Sunil to Rohan charging interest @ 10% per annum.

**Self – Balancing Ledgers**

9. From the following particulars, prepare Total Debtors Account in the general ledger:

Balance of Sundry Debtors as on 1-4-2017	Dr. (₹) 1,000
Transactions during April, 2017	₹
Sales (including cash ₹ 6,000)	22,000
Cash received from customers (in full settlement of claims of ₹ 13,000)	12,000
Bills receivable received	3,580
Bills receivable endorsed	800
Endorsed B/R dishonoured	300
B/R discounted	1,400
Bills receivable dishonoured	400
Interest charged on dishonoured B/R	30
Transfer from Debtors Ledger to Creditors Ledger	600

**Financial Statements of Not-For-Profit Organizations**

10. Following information has been given for Bharat Sports Club, Delhi for the year ending 31.12.2016 and 31.12.2017.

	31.12.2016	31.12.2017
Building (subject to 10% depreciation for the current year)	60,000	?
Furniture (subject to 10% depreciation for the current year)	-	20,000
Stock of Sports Materials	5,000	2,000
Prepaid Insurance	3,000	6,000
Subscription receivable	12,000	8,000
Advance Subscription	6,000	4,000
Locker Rent receivable	-	6,000
Advance Locker Rent received	-	2,000
Outstanding Rent for Godown	6,000	3,000
12% General Fund Investments	2,00,000	2,00,000
Accrued Interest on above	-	4,000
Cash Balance	1,000	64,000
Bank Balance	2,000	-
Bank Overdraft	-	2,000

**Additional Information:**

- (i) Entrance fees received ₹ 20,000, Life membership fees received ₹ 20,000 during the year.
- (ii) Surplus from Income and Expenditure Account ₹ 60,000.
- (iii) It is the policy of the club to treat 60% of entrance fees and 40% of life membership fees as revenue nature.
- (iv) The furniture was purchased on 01.01.2017.

Prepare Opening and Closing Balance Sheet of Bharat Sports Club as on 31<sup>st</sup> December, 2016 and 31<sup>st</sup> December, 2017 respectively.

**Accounts from Incomplete Records**

11. The following is the Balance Sheet of Manish and Suresh as on 1<sup>st</sup> April, 2016:

Liabilities	₹	Assets	₹
Capital:		Building	1,00,000
Manish	1,50,000	Machinery	65,000
Suresh	75,000	Stock	40,000
Creditors for goods	30,000	Debtors	50,000
Creditors for expenses	25,000	Bank	25,000
	<u>2,80,000</u>		<u>2,80,000</u>

They give you the following additional information:

- (i) Creditors' Velocity\* 1.5 month & Debtors' Velocity\* 2 months.
- (ii) Stock level is maintained uniformly in value throughout all over the year.
- (iii) Depreciation on machinery is charged @ 10%, Depreciation on building @ 5% in the current year.
- (iv) Cost price will go up 15% as compared to last year and also sales in the current year will increase by 25% in volume.
- (v) Rate of gross profit remains the same.
- (vi) Business Expenditures are ₹ 50,000 for the year. All expenditures are paid off in cash.
- (vii) Closing stock is to be valued on LIFO Basis.

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\* Velocity indicates the no. of times the creditors and debtors are turned over a year.

(viii) All sales and purchases are on credit basis and there are no cash purchases and sales.

Prepare Trading, Profit and Loss Account, Trade Debtors A/c and Trade Creditors A/c for the year ending 31.03.2017.

#### Hire Purchase Transactions

12. Srikumar bought 2 cars from 'Fair Value Motors Pvt. Ltd. on 1.4.2014 on the following terms (for both cars):

Down payment	6,00,000
1 <sup>st</sup> Installment at the end of first year	4,20,000
2 <sup>nd</sup> Installment at the end of 2 <sup>nd</sup> year	4,90,000
3 <sup>rd</sup> Installment at the end of 3 <sup>rd</sup> year	5,50,000

Interest is charged at 10% p.a.

Srikumar provides depreciation @ 25% on the diminishing balances.

On 31.3.2017 Srikumar failed to pay the 3<sup>rd</sup> installment upon which 'Fair Value Motors Pvt. Ltd.' repossessed 1 car. Srikumar agreed to leave one car with Fair Value Motors Pvt. Ltd. and adjusted the value of the car against the amount due. The car taken over was valued on the basis of 40% depreciation annually on written down basis. The balance amount remaining in the vendor's account after the above adjustment was paid by Srikumar after 3 months with interest @ 20% p.a.

You are required to:

- Calculate the cash price of the cars and the interest paid with each installment.
- Prepare Cars Account in the books of Srikumar assuming books are closed on March 31, every year.

Figures may be rounded off to the nearest rupee.

#### Investment Accounts

13. Alpha Ltd. purchased 5,000, 13.5% Debentures of Face Value of ₹ 100 each of Pergot Ltd. on 1<sup>st</sup> May 2017 @ ₹ 105 on cum interest basis. The interest on these instruments is payable on 31<sup>st</sup> & 30<sup>th</sup> of March & September respectively. On August 1<sup>st</sup> 2017 the company again purchased 2,500 of such debentures @ ₹ 102.50 each on cum interest basis. On October 1<sup>st</sup>, 2017 the company sold 2,000 Debentures @ ₹ 103 each on ex-interest basis. The market value of the debentures as at the close of the year was ₹ 106. Prepare the Debenture Investment Account in the books of Alpha Ltd. for the year ended 31<sup>st</sup> Dec. 2017 on Average Cost Basis.

**Insurance Claim for loss of stock**

14. The premises of Anmol Ltd. caught fire on 22<sup>nd</sup> January 2017, and the stock was damaged. The firm makes account up to 31<sup>st</sup> March each year. On 31<sup>st</sup> March, 2016 the stock at cost was ₹ 6,63,600 as against ₹ 4,81,100 on 31<sup>st</sup> March, 2015.

Purchases from 1<sup>st</sup> April, 2016 to the date of fire were ₹ 17,41,350 as against ₹ 22,62,500 for the full year 2015-16 and the corresponding sales figures were ₹ 24,58,500 and ₹ 26,00,000 respectively. You are given the following further information:

- (i) In July, 2016, goods costing ₹ 50,000 were given away for advertising purposes, no entries being made in the books.
- (ii) During 2016-17, a clerk had misappropriated unrecorded cash sales. It is estimated that the defalcation averaged ₹ 1,000 per week from 1<sup>st</sup> April, 2016 until the clerk was dismissed on 18<sup>th</sup> August, 2016.
- (iii) The rate of gross profit is constant.

From the above information calculate the stock in hand on the date of fire.

**Issues in Partnership Accounts**

15. A, B and C were partners sharing Profits and Losses in the ratio of 2 : 2 : 1. Their Balance Sheet as on 1.4.2015 stood as follows:

Liabilities	₹	Assets	₹
Capital Accounts:		Fixed Assets	10,00,000
5,00,000		Inventory	2,50,000
4,00,000		Trade Receivable	3,50,000
<u>3,00,000</u>	12,00,000	Cash and Bank	1,00,000
Reserves	1,00,000		
Trade Payables	<u>4,00,000</u>		
	17,00,000		<u>17,00,000</u>

On 1<sup>st</sup> October, 2015, C died. His representatives agreed that:

- (i) Goodwill of the firm be valued at ₹ 5,00,000. Goodwill not to be shown off in books of accounts.
- (ii) Fixed assets be written down by ₹ 1,00,000 and
- (iii) In lieu of profits, C should be paid at the rate of 25% p.a. on his capital as on 1.4.2015.

Current year's (2015-2016) profits after charging depreciation of ₹ 95,000 (₹ 50,000 related to the 1<sup>st</sup> half) was ₹ 4,05,000. Profit was evenly spread throughout the year.

As on 31.3.2016, the following were the balances:

Inventory	₹ 2,30,000
Trade Receivable	₹ 1,90,000
Trade Payable	₹ 3,50,000
Cash and Bank Balance	₹ 43,770

The particulars regarding their drawings are given below:

	Upto 1-10-2015	After 1-10-2015
A	41,250	50,000
B	41,250	50,000
C	17,500	-

You are required to:

- Prepare the Balance Sheet of the firm as on 31.3.2016, assuming that final settlement to C's executors was made on 31.3.2016.
- Prepare the Capital accounts of the partners as on 1.10.2015 & 31.3.2016.

#### Accounting in Computerized Environment

16. Recently a growing trend has developed for outsourcing the accounting function to a third party. What are the criteria based on which choice of such third party made?

#### Applicability of Accounting Standards

17. (a) List the criteria to be applied for rating a non-corporate entity as Level-II entity for the purpose of compliance of Accounting Standards in India.

#### AS 1 Disclosure of Accounting Policies

- (b) J Ltd. had made a rights issue of shares in 2016. In the offer document to its members, it had projected a surplus of ₹ 40 crores during the accounting year to end on 31st March, 2017. The draft results for the year, prepared on the hitherto followed accounting policies and presented for perusal of the board of directors showed a deficit of ₹ 10 crores. The board in consultation with the managing director, decided on the following:

- Value year-end inventory at works cost (₹ 50 crores) instead of the hitherto method of valuation of inventory at prime cost (₹ 30 crores).
- Provide for permanent fall in the value of investments - this fall had taken place over the past five years - the provision being ₹ 10 crores.

As chief accountant of the company, you are asked by the managing director to draft the notes on accounts for inclusion in the annual report for 2016-2017.



**AS 2 Valuation of Inventories**

18. (a) A private limited company manufacturing fancy terry towels had valued its closing inventory of inventories of finished goods at the realisable value, inclusive of profit and the export cash incentives. Firm contracts had been received and goods were packed for export, but the ownership in these goods had not been transferred to the foreign buyers.

Comment on the valuation of the inventories by the company.

**Depreciation Accounting as per AS 10 Property, Plant and Equipment**

- (b) In the year 2016-17, an entity has acquired a new freehold building with a useful life of 50 years for ₹ 90,00,000. The entity desires to calculate the depreciation charge per annum using a straight-line method. It has identified the following components (with no residual value of lifts & fixtures at the end of their useful life) as follows:

Component	Useful life (Years)	Cost
Land	Infinite	₹ 20,00,000
Roof	25	₹ 10,00,000
Lifts	20	₹ 5,00,000
Fixtures	10	₹ 5,00,000
Remainder of building	50	<u>₹ 50,00,000</u>
		<u>₹ 90,00,000</u>

Calculate depreciation for the year 2016-17 as per componentization method.

**AS 7 Construction Contracts**

19. (a) Uday Constructions undertake to construct a bridge for the Government of Uttar Pradesh. The construction commenced during the financial year ending 31.03.2016 and is likely to be completed by the next financial year. The contract is for a fixed price of ₹ 12 crores with an escalation clause. The costs to complete the whole contract are estimated at ₹ 9.50 crores of rupees. You are given the following information for the year ended 31.03.2016:

Cost incurred upto 31.03.2016 ₹ 4 crores

Cost estimated to complete the contract ₹ 6 crores

Escalation in cost by 5% and accordingly the contract price is increased by 5%.

You are required to ascertain the state of completion and state the revenue and profit to be recognized for the year as per AS 7.

**AS 9 Revenue Recognition**

- (b) A manufacturing company has the following stages of production and sale in manufacturing Fine paper rolls:

Date	Activity	Cost to Date (₹)	Net Realizable Value (₹)
15.1.16	Raw Material	1,00,000	80,000
20.1.16	Pulp (WIP 1)	1,20,000	1,20,000
27.1.16	Rough & thick paper (WIP 2)	1,50,000	1,80,000
15.2.16	Fine Paper Rolls	1,80,000	3,50,000
20.2.16	Ready for sale	1,80,000	3,50,000
15.3.16	Sale agreed and invoice raised	2,00,000	3,50,000
02.4.16	Delivered and paid for	2,00,000	3,50,000

Explain the stage on which you think revenue will be generated and state how much would be net profit for year ending 31.3.16 on this product according to AS 9.

**AS 10 Property, Plant and Equipment**

20. (a) Entity A, a supermarket chain, is renovating one of its major stores. The store will have more available space for in store promotion outlets after the renovation and will include a restaurant. Management is preparing the budgets for the year after the store reopens, which include the cost of remodeling and the expectation of a 15% increase in sales resulting from the store renovations, which will attract new customers.

Decide whether the remodeling cost will be capitalized or not.

**AS 13 Accounting for Investments**

- (b) How you will deal with the following in the financial statements of the Paridhi Electronics Ltd. as on 31.3.17 with reference to AS-13?

Paridhi Electronics Ltd. invested in the shares of another unlisted company on 1<sup>st</sup> May 2012 at a cost of ₹ 3,00,000 with the intention of holding more than a year. The published accounts of unlisted company received in January, 2017 reveals that the company has incurred cash losses with decline in market share and investment of Paridhi Electronics Ltd. may not fetch more than ₹ 45,000.

## ANSWERS

1.

Kapil Ltd.

**Balance Sheet**  
**as at 31<sup>st</sup> March, 2017**

	Particulars	Note No.	(₹)
<b>I</b>	<b>Equity and Liabilities</b>		
	<b>(1) Shareholders' Funds</b>		
	(a) Share Capital	1	19,90,000
	(b) Reserves and Surplus	2	59,586
	<b>(2) Current Liabilities</b>		
	(a) Trade Payables		2,40,500
	(b) Other Current Liabilities	3	13,28,000
	(c) Short-Term Provisions	4	<u>4,07,414</u>
	<b>Total</b>		<u>40,25,500</u>
<b>II</b>	<b>ASSETS</b>		
	<b>(1) Non-Current Assets</b>		
	(a) Fixed Assets		
	(i) Tangible Assets	5	29,30,000
	<b>(2) Current Assets</b>		
	(a) Inventories		7,08,000
	(b) Trade Receivables	6	3,59,500
	(c) Cash and Cash Equivalent	7	<u>28,000</u>
	<b>Total</b>		<u>40,25,500</u>

Kapil Ltd.

**Statement of Profit and Loss for the year ended 31<sup>st</sup> March, 2017**

	Particulars	Note No.	(₹)
I	Revenue from Operations		36,17,000
II	Other Income	8	<u>36,500</u>
<b>III</b>	<b>Total Revenue [I + II]</b>		<b><u>36,53,500</u></b>
IV	Expenses:		
	Cost of purchases		12,32,500

	Changes in Inventories [6,65,000-7,08,000]		(43,000)
	Employee Benefits Expenses	9	13,93,000
	Finance Costs	10	1,11,000
	Depreciation and Amortization Expenses		1,20,000
	Other Expenses	11	<u>4,40,000</u>
	<b>Total Expenses</b>		<b><u>32,53,500</u></b>
<b>V</b>	<b>Profit before Tax (III-IV)</b>		4,00,000
<b>VI</b>	<b>Tax Expenses @ 30%</b>		<u>(1,20,000)</u>
<b>VII</b>	<b>Profit for the period</b>		<u>2,80,000</u>

**Notes to Accounts:****1. Share Capital**

<b>Authorised Capital</b>	
5,00,000 Equity Shares of ₹ 10 each	<u>50,00,000</u>
<b>Issued Capital</b>	
2,00,000 Equity Shares of ₹ 10 each	20,00,000
<b>Subscribed Capital and fully paid</b>	
1,95,000 Equity Shares of ₹10 each	19,50,000
<b>Subscribed Capital but not fully paid</b>	
5,000 Equity Shares of ₹10 each ₹ 8 paid (Call unpaid ₹10,000)	<u>40,000</u> <u>19,90,000</u>

**2. Reserves and Surplus**

General Reserve		7,000
<b>Surplus i.e. Balance in Statement of Profit &amp; Loss:</b>		
Opening Balance	67,000	
Add: Profit for the period	2,80,000	
Less: Transfer to Reserve @ 2.5%	(7,000)	
Less: Equity Dividend [12% of (20,00,000-10,000)]	(2,38,800)	
Less: Corporate Dividend Tax (Working note)	<u>(48,614)</u>	<u>52,586</u>
		<u>59,586</u>

**3. Other Current Liabilities**

Bank Overdraft	12,67,000
Outstanding Expenses [25,000+36,000]	<u>61,000</u>
	<u>13,28,000</u>

**4. Short-term Provisions**

Provision for Tax	1,20,000
Equity Dividend payable	2,38,800
Corporate Dividend Tax	<u>48,614</u>
	<u>4,07,414</u>

**5. Tangible Assets**

Particulars	Value given (₹)	Depreciation rate	Depreciation Charged (₹)	Written down value at the end (₹)
Land	16,25,000		-	16,25,000
Plant & Machinery	7,50,000	5%	37,500	7,12,500
Furniture & Fixtures	1,50,000	10%	15,000	1,35,000
Patterns	3,75,000	10%	37,500	3,37,500
Engineering Tools	<u>1,50,000</u>	20%	<u>30,000</u>	<u>1,20,000</u>
	<u>30,50,000</u>		<u>1,20,000</u>	<u>29,30,000</u>

**6. Trade Receivables**

Trade receivables (4,00,500-16,000)	3,84,500
Less: Provision for doubtful debts	<u>(25,000)</u>
	<u>3,59,500</u>

**7. Cash & Cash Equivalent**

Cash Balance	8,000
Bank Balance in current A/c	<u>20,000</u>
	<u>28,000</u>

**8. Other Income**

Miscellaneous Income (Transfer fees)	6,500
Rental Income	<u>30,000</u>
	<u>36,500</u>

**9. Employee benefits expenses**

Wages	13,68,000
Add: Outstanding wages	<u>25,000</u>
	<u>13,93,000</u>

**10. Finance Cost**

Interest on Bank overdraft	1,11,000
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**11. Other Expenses**

Carriage Inward	57,500
Discount & Rebates	30,000
Advertisement	15,000
Rate, Taxes and Insurance	55,000
Repairs to Buildings	56,500
Commission & Brokerage	67,500
Miscellaneous Expenses [56,000+36,000] (Business Expenses)	92,000
Bad Debts [25,500+16,000]	41,500
Provision for Doubtful Debts	<u>25,000</u>
	<u>4,40,000</u>

**Working Note****Calculation of grossing-up of dividend:**

Particulars	₹
Dividend distributed by Company	2,38,800
Add: Increase for the purpose of grossing up of dividend $2,38,800 \times [15/(100-15)]$	<u>42,141</u>
Gross dividend	2,80,941
Dividend distribution tax @ 17.304%	48,614

**2. Cash flow statement (using direct method) for the year ended 31<sup>st</sup> March, 2017**

	(₹ in crores)	(₹ in crores)
<b>Cash flow from operating activities</b>		
Cash sales	262	
Cash collected from credit customers	134	
Less: Cash paid to suppliers for goods & services and to employees (Refer Working Note)	<u>(251)</u>	
Cash from operations	145	
Less: Income tax paid	<u>(26)</u>	
Net cash generated from operating activities		119
<b>Cash flow from investing activities</b>		

Net Payment for purchase of Machine (25 – 15)	(10)	
Proceeds from sale of investments	<u>16</u>	
Net cash used in investing activities		6
<b>Cash flow from financing activities</b>		
Redemption of Preference shares	(32)	
Proceeds from issue of Equity shares	24	
Debenture interest paid	(2)	
Dividend Paid	<u>(15)</u>	
<b>Net cash used in financing activities</b>		<u>(25)</u>
Net increase in cash and cash equivalents		100
Add: Cash and cash equivalents as on 1.04.2016		<u>2</u>
Cash and cash equivalents as on 31.3.2017		<u>102</u>

**Working Note:****Calculation of cash paid to suppliers of goods and services and to employees**

	(₹ in crores)
Opening Balance in creditors Account	84
Add: Purchases (220x .8)	<u>176</u>
Total	260
Less: Closing balance in Creditors Account	<u>92</u>
Cash paid to suppliers of goods	168
Add: Cash purchases (220x .2)	<u>44</u>
Total cash paid for purchases to suppliers (a)	212
Add: Cash paid to suppliers of other consumables and services (b)	19
Add: Payment to employees (c)	<u>20</u>
Total cash paid to suppliers of goods & services and to employees [(a)+ (b) + (c)]	<u>251</u>

3. **Statement showing the calculation of profits/losses for pre incorporation and Post incorporation period profits of Sanjana Ltd. for the year ended 31<sup>st</sup> March, 2017**

Particulars	Basis	Pre	Post
		₹	₹
Sales (given)		10,000	40,000

Less: Purchases	1:3.3	5,814	19,186
Carriage Inwards	1:3.3	<u>237</u>	<u>782</u>
Gross Profit (i)		<u>3,949</u>	<u>20,032</u>
Less: Selling Expenses	1:4	700	2,800
Preliminary Expenses			1,200
Salaries	1:3	900	2,700
Director Fees			1,200
Interest on capital		700	
Depreciation	1:3	700	2,100
Rent	1:3	<u>1,200</u>	<u>3,600</u>
Total of Expenses(ii)		<u>4,200</u>	<u>13,600</u>
Capital Loss/Net Profit (i-ii)		(251)	6,432

**Working Notes:**

1: Sales Ratio = 10,000 : 40,000 = 1 : 4

2: Time Ratio = 3:9 = 1:3

3: Purchase Price Ratio

∴ Ratio is 3 : 9

But purchase price was 10% higher in the company period

∴ Ratio is 3 : 9 + 10%

3:9.9 = 1:3.3.

**4. Journal Entries in the books of Manoj Ltd.**

			₹	₹
1-4-20X1	Equity share final call A/c	Dr.	5,40,000	
	To Equity share capital A/c			5,40,000
	(For final calls of ₹ 2 per share on 2,70,000 equity shares due as per Board's Resolution dated....)			
20-4-20X1	Bank A/c	Dr.	5,40,000	
	To Equity share final call A/c			5,40,000
	(For final call money on 2,70,000 equity shares received)			
	Securities Premium A/c	Dr.	75,000	
	Capital redemption reserve A/c	Dr.	1,20,000	



General Reserve A/c	Dr.	3,60,000	
Profit and Loss A/c (b.f.)	Dr.	1,20,000	
To Bonus to shareholders A/c (For making provision for bonus issue of one share for every four shares held)			6,75,000
Bonus to shareholders A/c	Dr.	6,75,000	
To Equity share capital A/c (For issue of bonus shares)			6,75,000

**Extract of Balance Sheet as at 30<sup>th</sup> April, 20X1 (after bonus issue)**

	₹
Authorised Capital	
30,000 12% Preference shares of ₹ 10 each	3,00,000
4,00,000 Equity shares of ₹ 10 each	<u>40,00,000</u>
Issued and subscribed capital	
24,000 12% Preference shares of ₹ 10 each, fully paid	2,40,000
3,37,500 Equity shares of ₹ 10 each, fully paid (Out of the above, 67,500 equity shares @ ₹ 10 each were issued by way of bonus shares)	33,75,000
Reserves and surplus	
Profit and Loss Account	4,80,000

**5. Journal Entries**

Particulars	Debit (₹)	Credit (₹)
First debentures A/c	Dr. 3,60,000	
Second debentures A/c	Dr. 3,60,000	
Unsecured trade payables A/c	Dr. 1,08,000	
To A (Being A's total liability ascertained)		8,28,000
A	Dr. 2,52,000	
To Capital reduction A/c (Being cancellation of debt up to ₹2,52,000)		2,52,000
Bank A/c	Dr. 36,000	
To A (Being cash received in course of settlement)		36,000

A	Dr.	6,12,000	
To First debentures A/c			6,12,000
(Being liability of A, discharged against first debentures)			
Second debentures A/c	Dr.	3,60,000	
Unsecured trade payables A/c	Dr.	72,000	
To B			4,32,000
(Being B's liability ascertained)			
B	Dr.	4,32,000	
To Bank A/c			1,08,000
To Capital reduction A/c			3,24,000
(Being B's liability discharged in satisfaction of all claims)			
Unsecured trade payables A/c	Dr.	3,60,000	
To Equity share capital A/c			1,62,000
To Loan (Unsecured) A/c			1,44,000
To Capital reduction A/c			54,000
(Being settlement of unsecured Trade payables)			
Share call A/c	Dr.	3,20,000	
To Share capital A/c			3,20,000
(Being final call money due)			
Bank A/c	Dr.	3,20,000	
To Share call A/c			3,20,000
(Being final call money received)			
Capital reduction A/c	Dr.	6,30,000	
To Capital reserve A/c			6,30,000
(Being balance in capital reduction account transferred to capital reserve account)			

**Working Note:**

	Settlement of claim of remaining unsecured trade payables	₹
	60% of ₹ 3,60,000	2,16,000
	Considering their claim for share of ₹ 100 each	
	$2,16,000/100 = 2,160$ shares	
	Less: Number of shares to be issued	

2,160 x 3= 6,480 shares of ₹25 each	(1,62,000)
Transferred to Capital reduction A/c	<u>54,000</u>

**6. Balance Sheet of AB Ltd.**

Particulars	Notes	₹
<b>Equity and Liabilities</b>		
1 Shareholders' funds		
a Share capital	1	30,80,000
b Reserves and Surplus	2	6,17,100
2 Current liabilities		
a Other liabilities		38,900
Total		<u>37,36,000</u>
<b>Assets</b>		
1 Non-current assets		
a Fixed assets		
Tangible assets	3	23,09,000
Intangible assets	4	1,12,000
b Non-current investments		1,55,000
2 Current assets		
a Inventories (3,58,000 + 2,40,000)		5,98,000
b Trade receivables (72,000 +70,000)		1,42,000
c Cash and cash equivalents		4,20,000
Total		<u>37,36,000</u>

**Notes to accounts**

		₹
<b>1 Share Capital</b>		
Authorized share capital		
3,00,000 equity shares of ₹ 10 each	30,00,000	
60,000, 8% cumulative Preference Shares of ₹ 10 each	<u>6,00,000</u>	<u>36,00,000</u>
Equity share capital		

2,48,000 equity shares of ₹ 10 each (of the above shares, 2,18,000 shares have been issued for consideration other than cash)		24,80,000
Preference share capital		
60,000, 8% cumulative Preference Shares of ₹ 10 each		6,00,000
Total		30,80,000
<b>2 Reserves and Surplus</b>		
Debit balance of Profit and Loss Account		
Underwriting commission	38,900	
Preliminary expenses	<u>24,000</u>	(62,900)
Securities Premium A/c		
(2,48,000 equity shares x 2.50)	6,20,000	
(60,000 Preference shares x ₹ 1)	<u>60,000</u>	6,80,000
		6,17,100
<b>3 Tangible assets</b>		
Building	5,40,000	
Motor car	1,26,000	
Plant & machinery	15,10,000	
Furniture	<u>1,33,000</u>	23,09,000
<b>4 Intangible assets</b>		
Goodwill (W.N. 4) (15,000 + 62,000-65,000)	12,000	
Patents	<u>1,00,000</u>	1,12,000

**Working Notes:****1. Mode of discharge of Purchase Consideration of A Ltd.**

	₹
Cash payment	5,75,000
Equity shares (1,80,000 Shares x ₹ 12.5)	<u>22,50,000</u>
Total Purchase consideration	<u>28,25,000</u>

**2. Mode of discharge of Purchase Consideration of B Ltd.**

	₹
Cash payment	16,000

Equity shares (38,000 shares x ₹ 12.5)	<u>4,75,000</u>
Total Purchase consideration	<u>4,91,000</u>

## 3. Cash at bank balance in the initial balance sheet of AB Ltd.

## Cash and Bank Account

	₹		₹
To Issue of preference shares (60,000 x 11)	6,60,000	By Payment to A ltd.	5,75,000
To Equity shares (30,000 x 12.50)	<u>3,75,000</u>	By Payment to B ltd.	16,000
	<u>10,35,000</u>	By Preliminary expenses	24,000
		By Balance c/d	<u>4,20,000</u>
			<u>10,35,000</u>

## 4. Calculation of goodwill/ capital reserve of A Ltd. &amp; B Ltd.

Particulars	A Ltd.		B Ltd.	
Business Purchase A/c		28,25,000		4,91,000
Less: Goodwill			62,000	
Patent A/c	1,00,000		-	
Building A/c	5,40,000		-	
Plant & Mach. A/c	15,10,000		-	
Motor car A/c	-		1,26,000	
Furniture A/c	75,000		58,000	
Investment A/c	1,55,000		-	
Stocks A/c	3,58,000		2,40,000	
Debtors A/c	<u>72,000</u>	<u>(28,10,000)</u>	<u>70,000</u>	<u>(5,56,000)</u>
Goodwill / Capital reserve (Bal. fig.)		<u>15,000</u>		<u>(65,000)</u>
Net goodwill (15,000 +62,000 -65,000) = 12,000				

## Note:

It has been assumed in the above solution that preliminary expenses of ₹ 24,000 has been paid and underwriting commission is still payable in the balance sheet of the amalgamated company.

## 7. Calculation of the average due date

Taking 4<sup>th</sup> July as the base date

Sl. No.	Date of bill	Due Date of Maturity	Amount ₹	No. of days from starting date (4 <sup>th</sup> July)	Product
1	1 <sup>st</sup> May 2017	4th July	500	0	0
2	10th May 2017	13th August	300	40	12,000
3	5th June 2017	8th August	400	35	14,000
4	25th June 2017	28 <sup>th</sup> July	375	24	9,000
5	10th July 2017	13th September	<u>500</u>	71	<u>35,500</u>
Total			<u>2,075</u>		<u>70,500</u>

Average Due Date is  $70,500/2,075 = 34$  days after the assumed due date, 4th July, 2017.  
The new bill should be for ₹ 2,075 payable on 7<sup>th</sup> August, 2017.

## 8.

**In the books of Sunil**  
**Rohan in Account Current with Sunil**  
**as on 30<sup>th</sup> June, 2017**

Date 2017	Particulars	Amount ₹	Days	Interest ₹	Date 2017	Particulars	Amount ₹	Days	Interest ₹
Feb. 16	To Sales	6,480.00	134	237.90	Jan. 1	By Balance b/d	3,010.00	181	149.26
Mar. 24	To Sales	3,560.00	98	95.58	Jan. 7	By Purchases	4,430.00	174	211.18
June 22	To Sales	2,280.00	8	5.00	Feb. 18	By Returns inward	560.00	132	20.25
June 30	To Balance of interest			107.08	Apr. 22	By B/R (maturing on 25 July, 2017)	1,500.00	(25)	(10.27)*
June 30	To Balance c/d	2,497.08			Apr. 29	By Cash	2,500.00	62	42.47
					May 17	By Purchases	2,710.00	44	32.67
					June 30	By Interest	107.08		
		<u>14,817.08</u>		<u>445.56</u>			<u>14,817.08</u>		<u>445.56</u>
					July 1	By Balance b/d	2,497.08		

\*Interest on amount of Bill receivable maturing on 25<sup>th</sup> July, 2017 is a red ink interest.

Credit for the B/R is given on the date when it is received, but the amount will be received only on its maturity. Hence, the interest for the period for which the bill is to run after accounting period is shown as negative figure.

9. **Total Debtors Account in General Ledger**

2017	Particulars	₹	2017	Particulars	₹
April 1	To Balance b/d	1,000			
April 30	To Sales (Credit)	16,000	April 30	By Cash	12,000
	To Total creditors (endorsed B/R dishonoured)	300		By Discount	1,000
	To B/R (Dishonoured)	400		By Bills receivable	3,580
	To Interest	30		By Total creditors (Transfer)	600
		17,730		By Balance c/d	550
					17,730

**Notes:**

1. B/R discounted and Cash sales will not be shown in the Total Debtors
2. Endorsed B/R dishonoured and transfers will be shown in the Total Debtors.

10. **Balance Sheet of Bharat Sports club as at 31<sup>st</sup> December, 2016**

Liabilities	₹	Assets	₹
Outstanding Rent	6,000	Building	60,000
Advance Subscription	6,000	Stock of Sports materials	5,000
Capital Fund (balancing Figure)	2,71,000	Prepaid Insurance	3,000
		Subscription receivable	12,000
		12% General Fund Investments	2,00,000
		Cash Balance	1,000
		Bank Balance	2,000
	<u>2,83,000</u>		<u>2,83,000</u>

**Balance Sheet of Bharat Sports club as at 31<sup>st</sup> December, 2017**

Liabilities		₹	Assets		₹
Outstanding Rent		3,000	Building		
Advance Subscription		4,000	Book Value	60,000	
Advance Locker Rent		2,000	Less: Depreciation	<u>6,000</u>	54,000
Bank Overdraft		2,000	Furniture Cost	20,000	
Capital Fund:			Less: Depreciation	<u>2,000</u>	18,000
Opening Balance	2,71,000		Stock of sports materials		2,000

Add: Entrance Fees [20,000 x 40%]	8,000		Prepaid Insurance	6,000
Add: Life Membership fee [₹ 20,000 x 60%]	12,000		Subscription receivable	8,000
Add: Surplus	<u>60,000</u>	3,51,000	Locker Rent receivable	6,000
			12% General	2,00,000
			Fund Investments	
			Accrued Interest on 12%	
			General Fund Investments	4,000
			Cash Balance	<u>64,000</u>
		<u>3,62,000</u>		3,62,000

11.

**Trading and Profit and Loss account  
for the year ending 31st March, 2017**

Particulars	₹	Particulars	₹
To Opening Stock	40,000	By Sales	4,31,250
To Purchases (Working Note)	3,45,000	By Closing Stock	40,000
To Gross Profit c/d (20% on sales)	<u>86,250</u>		
	<u>4,71,250</u>		<u>4,71,250</u>
To Business Expenses	50,000	By Gross Profit b/d	86,250
To Depreciation on:			
Machinery	6,500		
Building	<u>5,000</u>		
To Net profit	<u>24,750</u>		
	<u>86,250</u>		<u>86,250</u>

**Trade Debtors Account**

Particulars	₹	Particulars	₹
To Balance b/d	50,000	By Bank (bal.fig.)	4,09,375
To Sales	<u>4,31,250</u>	By Balance c/d (1/6 of 4,31,250)	<u>71,875</u>
	<u>4,81,250</u>		<u>4,81,250</u>



## Trade Creditors Account

Particulars		₹	Particulars		₹
To	Bank (Balancing figure)	3,31,875	By	Balancing b/d	30,000
To	Balance c/d/ (1/8 of ₹ 3,45,000)	<u>43,125</u>	By	Purchases	<u>3,45,000</u>
		<u>3,75,000</u>			<u>3,75,000</u>

## Working Note:

		₹
(i)	Calculation of Rate of Gross Profit earned during previous year	
A	Sales during previous year (₹ 50,000 x 12/2)	3,00,000
B	Purchases (₹ 30,000 x 12/1.5)	2,40,000
C	Cost of Goods Sold (₹ 40,000 + ₹ 2,40,000 – ₹ 40,000)	2,40,000
D	Gross Profit (A-C)	60,000
E	Rate of Gross Profit $\frac{₹ 60,000}{₹ 3,00,000} \times 100$	20%
(ii)	Calculation of sales and Purchases during current year	₹
A	Cost of goods sold during previous year	2,40,000
B	Add: Increases in volume @ 25 %	<u>60,000</u>
		3,00,000
C	Add: Increase in cost @ 15%	<u>45,000</u>
D	Cost of Goods Sold during Current Year	3,45,000
E	Add: Gross profit @ 25% on cost (20% on sales)	<u>86,250</u>
F	Sales for current year [D+E]	<u>4,31,250</u>

## 12. (i) Calculation of Interest and Cash Price

No. of installments	Outstanding balance at the end after the payment of installment	Amount due at the time of installment	Outstanding balance at the end before the payment of installment	Interest	Outstanding balance at the beginning
[1]	[2]	[3]	[4] = 2 + 3	[5] = 4 x 10/110	[6] 4-5
3 <sup>rd</sup>	-	5,50,000	5,50,000	50,000	5,00,000
2 <sup>nd</sup>	5,00,000	4,90,000	9,90,000	90,000	9,00,000
1 <sup>st</sup>	9,00,000	4,20,000	13,20,000	1,20,000	12,00,000

Total cash price = ₹ 12,00,000+ 6,00,000 (down payment) = ₹ 18,00,000.

(ii) In the books of Srikumar  
Cars Account

Date	Particulars	₹	Date	Particulars	₹
1.4.2014	To Fair Value Motors A/c	18,00,000	31.3.2015	By Depreciation A/c	4,50,000
				By Balance c/d	13,50,000
		18,00,000			18,00,000
1.4.2015	To Balance b/d	13,50,000	31.3.2016	By Depreciation A/c	3,37,500
				By Balance c/d	10,12,500
		13,50,000			13,50,000
1.4.2016	To Balance b/d	10,12,500	31.3.2017	By Depreciation A/c	2,53,125
				By Fair Value Motors A/c (Value of 1 Car taken over after depreciation for 3 years @ 40% p.a.) [9,00,000 - (3,60,000 + 2,16,000 + 1,29,600)]	1,94,400
				By Loss transferred to Profit and Loss A/c on surrender (Bal. fig.)	1,85,288
				By Balance c/d $\frac{1}{2} (10,12,500 - 2,53,125)$	3,79,687
		10,12,500			10,12,500

13.

## Books of Alpha Ltd.

## Investment in 13.5% Debentures in Pergot Ltd. Account

(Interest payable on 31<sup>st</sup> March & 30<sup>th</sup> September)

Date	Particulars	Nominal	Interest	Amount	Date	Particulars	Nominal	Interest	Amount
2017		₹	₹	₹	2017		₹	₹	₹
May 1	To Bank	5,00,000	5,625	5,19,375	Sept.30	By Bank (6 months Int)		50,625	
Aug.1	To Bank	2,50,000	11,250	2,45,000	Oct.1	By Bank	2,00,000		2,06,000
Oct.1	To P&L A/c			2,167					
Dec.31	To P&L A/c		52,313		Dec.31	By Balance c/d	5,50,000	18,563	5,60,542
		<u>7,50,000</u>	<u>69,188</u>	<u>7,66,542</u>			<u>7,50,000</u>	<u>69,188</u>	<u>7,66,542</u>

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

**Working Notes:**

1. Interest paid on ₹ 5,00,000 purchased on May 1<sup>st</sup>, 2017 for the month of April 2017, as part of purchase price:  $5,00,000 \times 13.5\% \times 1/12 = ₹ 5,625$
2. Interest received on 30<sup>th</sup> Sept. 2017
  - On ₹ 5,00,000 =  $5,00,000 \times 13.5\% \times \frac{1}{2} = 33,750$
  - On ₹ 2,50,000 =  $2,50,000 \times 13.5\% \times \frac{1}{2} = \underline{16,875}$
  - Total ₹ 50,625
3. Interest paid on ₹ 2,50,000 purchased on Aug. 1<sup>st</sup> 2017 for April 2017 to July 2017 as part of purchase price:
  - $2,50,000 \times 13.5\% \times 4/12 = ₹ 11,250$
4. Loss on Sale of Debentures
  - Cost of acquisition
  - (₹ 5,19,375 + ₹ 2,45,000) x ₹ 2,00,000/₹ 7,50,000 = 2,03,833
  - Less: Sale Price (2,000 x 103) = 2,06,000
  - Profit on sale = ₹ 2,167
5. Cost of Balance Debentures
  - (₹ 5,19,375 + ₹ 2,45,000) x ₹ 5,50,000/₹ 7,50,000 = ₹ 5,60,542
6. Interest on Closing Debentures for period Oct.-Dec. 2017 carried forward (accrued interest)
  - ₹ 5,50,000 x 13.5% x 3/12 = ₹ 18,563

**14. Ascertainment of rate of gross profit for the year 2015-16**  
**Trading A/c for the year ended 31-3-2016**

	₹		₹
To Opening stock	4,81,100	By Sales	26,00,000
To Purchases	22,62,500	By Closing stock	6,63,600
To Gross profit	5,20,000		
	<u>32,63,600</u>		<u>32,63,600</u>

$$\begin{aligned} \text{Rate of gross profit} &= \frac{\text{GP}}{\text{Sales}} \times 100 \\ &= \frac{5,20,000}{26,00,000} \times 100 = 20\% \end{aligned}$$

**Memorandum Trading A/c for the period from 1-4-2016 to 22-01-2017**

	₹	₹		₹	₹
To Opening stock		6,63,600	By Sales	24,58,500	
To Purchases	17,41,350		Add: Unrecorded cash sales (W.N.)	<u>20,000</u>	24,78,500
Less: Goods used for advertisement	<u>(50,000)</u>	16,91,350	By Closing stock		3,72,150
To Gross profit (20% of ₹ 24,78,500)		4,95,700			
		<u>28,50,650</u>			<u>28,50,650</u>

Estimated stock in hand on the date of fire was ₹ 3,72,150.

**Working Note:****Cash sales defalcated by the Accountant:**

Defalcation period = 1.4.2016 to 18.8.2016 = 140 days

Since, 140 days / 7 weeks = 20 weeks

Therefore, amount of defalcation = 20 weeks × ₹ 1,000 = ₹ 20,000.

**15. (i) Balance Sheet as on 31<sup>st</sup> March, 2016**

Liabilities		₹	₹	Assets		₹	₹
Capital Accounts				Fixed Assets		10,00,000	
A	5,09,385			Less: Written down	<u>(1,00,000)</u>		
B	<u>4,09,385</u>	9,18,770				9,00,000	
Trade Payables	3,50,000			Less: Depreciation	<u>(95,000)</u>		8,05,000
				Trade Receivables			1,90,000
				Inventory			2,30,000
				Cash and Bank			<u>43,770</u>
			<u>12,68,770</u>				<u>12,68,770</u>

**(ii) Partners' Capital Accounts as on 1-10-2015**

		A	B	C		A	B	C	
To	Revaluation A/c (Loss of Fixed Assets)	40,000	40,000	20,000	By	Balance b/d	5,00,000	4,00,000	3,00,000
To	Drawings	41,250	41,250	17,500	By	Reserves	40,000	40,000	20,000
To	C	50,000	50,000	-	By	A & B (goodwill adjustment)	-	-	1,00,000

To	Executor's A/c	-	-	4,20,000	By	Profit and Loss Appropriation A/c (W.N.2)	81,250	81,250	37,500
To	Balance c/d	<u>4,90,000</u>	<u>3,90,000</u>	-					
		6,21,250	5,21,250	4,57,500			6,21,250	5,21,250	4,57,500

**Partners' Capital Accounts as on 31-3-2016**

Dr.		A		B		Cr.		A		B	
To	Drawings	50,000		50,000		By	Balance b/d	4,90,000		3,90,000	
To	Balance c/d	5,09,385		4,09,385		By	Profit & Loss Appropriation A/c	69,385		69,385	
		<u>5,59,385</u>		<u>4,59,385</u>				<u>5,59,385</u>		<u>4,59,385</u>	

**Working Notes:**

**1. Calculation of profits**

	₹
(a) Profit after Depreciation	4,05,000
Add: Depreciation	<u>95,000</u>
Profit before Depreciation	<u>5,00,000</u>
(b) Profit for the 1st half (evenly spread)	2,50,000
Less: Depreciation with respect to 1st half	<u>(50,000)</u>
Post Depreciation profit	<u>2,00,000</u>
(c) Profit for the 2nd half	2,50,000
Less: Depreciation for the 2nd half	<u>(45,000)</u>
2nd half profit after Depreciation	<u>2,05,000</u>

**2. Profit and Loss Appropriation A/c (for the first half)**

Dr.		₹		₹		Cr.		₹	
To	Interest on C Capital (3,00,000 × 25% for 6 months)		37,500	By	Profit		2,00,000		

To	A	81,250		
	B	<u>81,250</u>	<u>1,62,500</u>	
			<u>2,00,000</u>	<u>2,00,000</u>

### 3. Application of Section 37 of the Partnership Act

Either

$$(i) \text{ Interest on } 4,20,000 \times \frac{6}{100} \times \frac{6}{12} = ₹ 12,600$$

Or

(ii) Profit earned out of unsettled capital

$$2,05,000 \times \frac{4,20,000}{(4,90,000 + 3,90,000 + 4,20,000)} = ₹ 66,230$$

In the absence of specific agreement amongst partners on the above subject matter, the representatives of the deceased partner can receive at their option, interest at the rate of 6% p.a. or the share of profit earned for the amount due to the deceased partner.

In the given case, it would be rational to assume that the representatives would opt for ₹ 66,230.

### 4. Profit and Loss Appropriation A/c for the second half

Dr.		Cr.		
		₹	₹	
To	Executors A/c	66,230	By Net Profit	2,05,000
To	A	69,385		
	B	<u>69,385</u>		
		<u>1,38,770</u>		
		<u>2,05,000</u>		<u>2,05,500</u>

### 5. C's Executors Account

Dr.		Cr.		
To	Bank	4,86,230	By C's Capital A/c	4,20,000
			By Profit & Loss Appropriation	<u>66,230</u>
		<u>4,86,230</u>		<u>4,86,230</u>

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

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

1. The type of services provided and whether the same matches with the requirements,
  2. The reputation and background of the vendor,
  3. The comparative costs of the various propositions,
  4. The assurance of quality.
17. (a) Non-corporate entities which are not level I entities but fall in any one or more of the following categories are classified as level II entities:
- (i) All commercial, industrial and business reporting entities, whose turnover (excluding other income) exceeds rupees one crore but does not exceed rupees fifty crore in the immediately preceding accounting year.
  - (ii) All commercial, industrial and business reporting entities having borrowings (including public deposits) in excess of rupees one crore but not in excess of rupees ten crore at any time during the immediately preceding accounting year.
  - (iii) Holding and subsidiary entities of any one of the above.
- (b) As per AS 1, any change in the accounting policies which has a material effect in the current period or which is reasonably expected to have a material effect in later periods should be disclosed. In the case of a change in accounting policies which has a material effect in the current period, the amount by which any item in the financial statements is affected by such change should also be disclosed to the extent ascertainable. Where such amount is not ascertainable, wholly or in part, the fact should be indicated. Accordingly, the notes on accounts should properly disclose the change and its effect.

**Notes on Accounts:**

- (i) During the year inventory has been valued at factory cost, against the practice of valuing it at prime cost as was the practice till last year. This has been done to take cognizance of the more capital intensive method of production on account of heavy capital expenditure during the year. As a result of this change, the year-end inventory has been valued at ₹ 50 crores and the profit for the year is increased by ₹ 20 crores.
- (ii) The company has decided to provide ₹ 10 crores for the permanent fall in the value of investments which has taken place over the period of past five years. The provision so made has reduced the profit disclosed in the accounts by ₹ 10 crores.

- 18 (a) Accounting Standard 2 "Valuation of Inventories" states that inventories should be valued at lower of historical cost and net realizable value. The standard states, "at certain stages in specific industries, such as when agricultural crops have been harvested or mineral ores have been extracted, performance may be substantially complete prior to the execution of the transaction generating revenue. In such cases, when sale is assured under forward contract or a government guarantee or when market exists and there is a negligible risk of failure to sell, the goods are often valued at net realisable value at certain stages of production."

Terry Towels do not fall in the category of agricultural crops or mineral ores. Accordingly, taking into account the facts stated, the closing inventory of finished goods (Fancy terry towel) should have been valued at lower of cost and net realisable value and not at net realisable value. Further, export incentives are recorded only in the year the export sale takes place. Therefore, the policy adopted by the company for valuing its closing inventory of inventories of finished goods is not correct.

- (b) Statement showing amount of depreciation as per Componentization Method

Component	Depreciation (Per annum) (₹)
Land	Nil
Roof	40,000
Lifts	25,000
Fixtures	50,000
Remainder of Building	<u>1,00,000</u>
	<u>2,15,000</u>

**Note:** When the roof requires replacement at the end of its useful life the carrying amount will be nil. The cost of replacing the roof should be recognised as a new component.

19. (a)

	₹ in crore
Cost of construction of bridge incurred 31.3.16	4.00
Add: Estimated future cost	<u>6.00</u>
Total estimated cost of construction	<u>10.00</u>
Contract Price (12 crore x 1.05)	12.60 crore

**Stage of completion**

Percentage of completion till date to total estimated cost of construction

$$= (4/10) \times 100 = 40\%$$



**Revenue and Profit to be recognized for the year ended 31<sup>st</sup> March, 2016 as per AS 7**

Proportion of total contract value recognized as revenue = Contract price x percentage of completion

= ₹ 12.60 crore x 40% = ₹ 5.04 crore

Profit for the year ended 31<sup>st</sup> March, 2016 = ₹ 5.04 crore less ₹ 4 crore = 1.04 crore

- (b) According to AS 9 “Revenue Recognition”, in a transaction involving the sale of goods, performance should be regarded as being achieved when the following conditions have been fulfilled:
- (i) the seller of goods has transferred to the buyer the property in the goods for a price or all significant risks and rewards of ownership have been transferred to the buyer and the seller retains no effective control of the goods transferred to a degree usually associated with ownership; and
  - (ii) no significant uncertainty exists regarding the amount of the consideration that will be derived from the sale of the goods.

Thus, sales will be recognized only when following two conditions are satisfied:

- (i) The sale value is fixed and determinable.
- (ii) Property of the goods is transferred to the customer.

Both these conditions are satisfied only on 15.3.2016 when sales are agreed upon at a price and goods are allocated for delivery purpose through invoice. The amount of net profit ₹ 1,50,000 (3,50,000 – 2,00,000) would be recognized in the books for the year ending 31<sup>st</sup> March, 2016.

20. (a) The expenditure in remodelling the store will create future economic benefits (in the form of 15% of increase in sales). Moreover, the cost of remodelling can be measured reliably, therefore, it should be capitalized in line with AS 10 PPE.
- (b) As per AS 13, “Accounting for Investments” Investments classified as long term investments should be carried in the financial statements at cost. However, provision for diminution shall be made to recognise a decline, other than temporary, in the value of the investments, such reduction being determined and made for each investment individually. The standard also states that indicators of the value of an investment are obtained by reference to its market value, the investee's assets and results and the expected cash flows from the investment.

On this basis, the facts of the case given in the question clearly suggest that the provision for diminution should be made to reduce the carrying amount of shares to ₹ 45,000 in the financial statements for the year ended 31<sup>st</sup> March, 2017 and charge the difference of loss of ₹ 2,55,000 to profit and loss account.

**AS 10: PROPERTY, PLANT AND EQUIPMENT****1. Introduction**

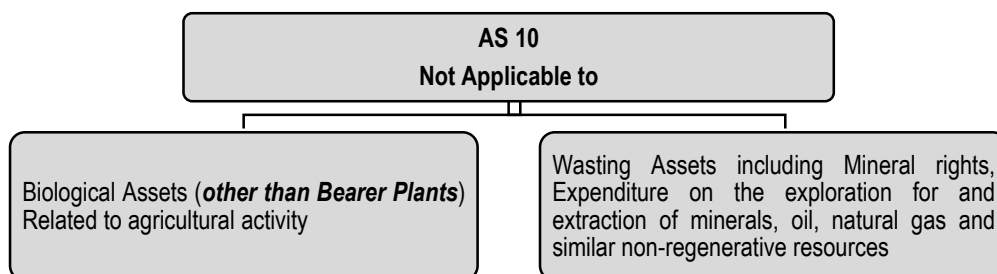
The objective of this Standard is to prescribe Accounting treatment for Property, Plant and Equipment (PPE). The principal issues in accounting for property, plant and equipment are the recognition of the assets, the determination of their carrying amounts and the depreciation charges and impairment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

**2. Scope of the Standard**

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

**Exception:**

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

**This Standard does not apply to:**

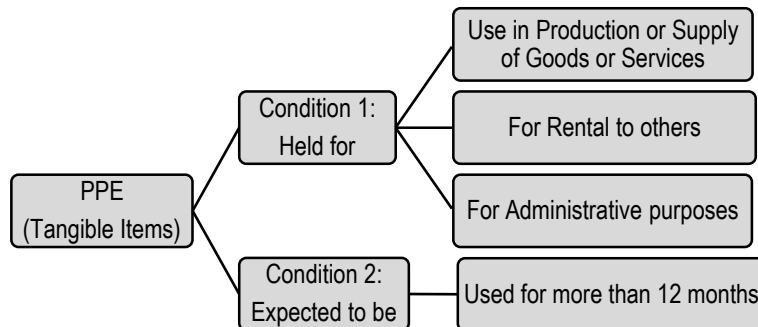
**Note:** AS 10 applies to Bearer Plants but it does not apply to the produce on Bearer Plants.

**Clarifications:**

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

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

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



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

**“Administrative purposes”:** The term ‘Administrative purposes’ has been used in **wider sense** to **include all business purposes**. Thus, PPE would include assets used for:

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

of an Enterprise.

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

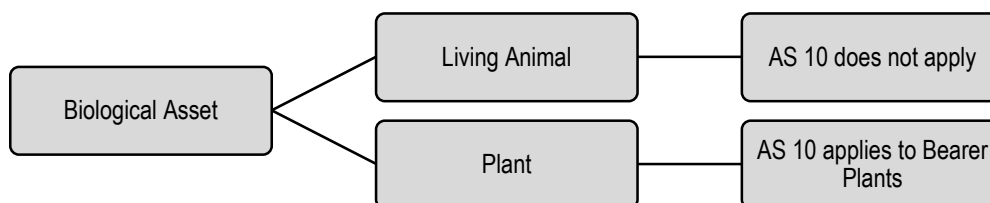
The acquisition of such PPE, although not directly increasing the future economic benefits of any particular existing item of PPE, may be necessary for an enterprise to obtain the future economic benefits from its other assets.

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

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

#### 4. Other Definitions

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



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

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

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

**The following are not Bearer Plants:**

- (a) Plants cultivated to be **harvested** as Agricultural produce  
**Example:** Trees grown for use as lumber
- (b) Plants cultivated **to produce** Agricultural produce when there is more than a remote likelihood that the entity will **also harvest and sell** the plant as agricultural produce, other than as incidental scrap sales  
**Example:** Trees which are cultivated both for their fruit and their lumber
- (c) Annual crops  
**Example:** Maize and wheat

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

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

- Biological transformation; and

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

## 5. Recognition Criteria for PPE

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

- (a) It is probable that future economic benefits associated with the item will flow to the enterprise, and
- (b) The cost of the item can be measured reliably.

### Notes:

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

### When do we apply the above criteria for Recognition?

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

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

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

- Recognised as PPE as per AS 10

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

- Such items are classified as Inventory as per AS 2

## 7. Treatment of Subsequent Costs

### Cost of day-to-day servicing

#### Meaning:

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

#### Accounting Treatment:

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

### Replacement of Parts of PPE

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

#### Examples:

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

#### Accounting Treatment:

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

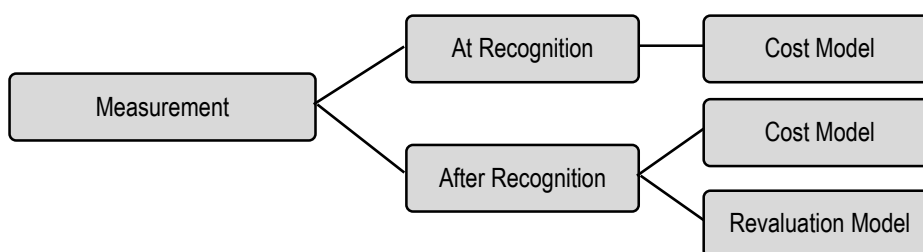
**Note:** The carrying amount of those parts that are **replaced is derecognised** in accordance with the de-recognition provisions of this Standard.

#### Regular Major Inspections - Accounting Treatment

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

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

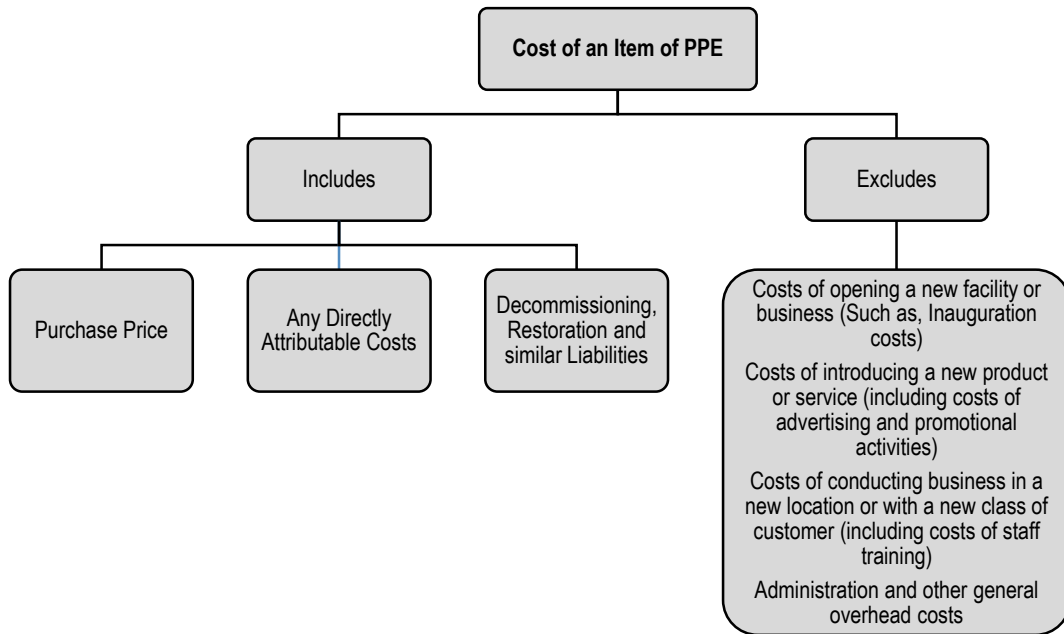
### 8. Measurement of PPE



### 9. Measurement at Recognition

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

**What are the elements of Cost?**

**Cost of an item of PPE comprises:****Examples of directly attributable costs are:**

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

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

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

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

**C. Decommissioning, Restoration and similar Liabilities:**

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

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

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

**10. Cost of a Self-constructed Asset**

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

1. If an enterprise makes similar assets for sale in the normal course of business, the cost of the asset is usually the same as the cost of constructing an asset for sale (see AS 2). Therefore, any **internal profits are eliminated** in arriving at such costs.
2. Cost of **abnormal amounts** of wasted material, labour, or other resources incurred in self constructing an asset is **not included** in the cost of the asset.
3. AS 16\* on Borrowing Costs, establishes criteria for the **recognition of interest** as a component of the carrying amount of a self-constructed item of PPE.

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

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



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

#### 11. Measurement of Cost

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

##### A. If payment is deferred beyond normal credit terms:

Total payment - Cash price equivalent

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

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

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

- (a) Exchange transaction lacks commercial substance; Or
- (b) Fair value of neither the asset(s) received nor the asset(s) given up is reliably measurable.

##### Note:

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

##### C. PPE purchased for a Consolidated Price:

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

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

#### 12. Measurement after Recognition

An enterprise should choose

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

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

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

**Examples of separate classes:**

- (a) Land
- (b) Land and Buildings
- (c) Machinery
- (d) Ships
- (e) Aircraft
- (f) Motor Vehicles
- (g) Furniture and Fixtures
- (h) Office Equipment
- (i) Bearer plants

**Cost Model**

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

Cost - Any Accumulated Depreciation - Any Accumulated Impairment losses

**Revaluation Model**

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

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

**Revaluation for entire class of PPE**

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

**Frequency of Revaluations**

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

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

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

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

Annual revaluation shall be done.

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

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

**Determination of Fair Value**

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

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

**Example:**

Based on

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

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

**13. Accounting Treatment of Revaluations**

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

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

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

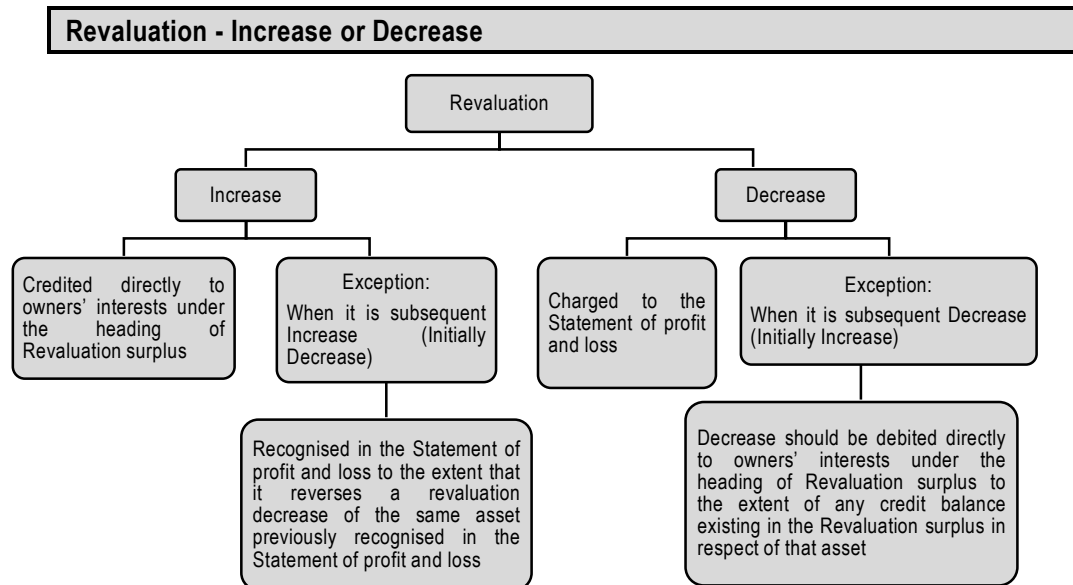
Gross carrying amount

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

**Accumulated depreciation at the date of the revaluation is**

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

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



### Treatment of Revaluation Surplus

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

#### Case I : When whole surplus is transferred:

When the asset is:

- Retired; Or
- Disposed of

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

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

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

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

## 14. Depreciation

### Component Method of Depreciation:

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

### Depreciable Amount and Depreciation Period

### What is “Depreciable Amount”?

#### Depreciable amount is:

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

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

### Review of Residual Value and Useful Life of an Asset

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

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

#### Commencement of period for charging Depreciation

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

#### Cessation of Depreciation

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

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

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

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

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

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

#### Land and Buildings

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

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

**Exceptions:** Quarries and sites used for landfill.

**Depreciation on Land:****I. If land itself has a limited useful life:**

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

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

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

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

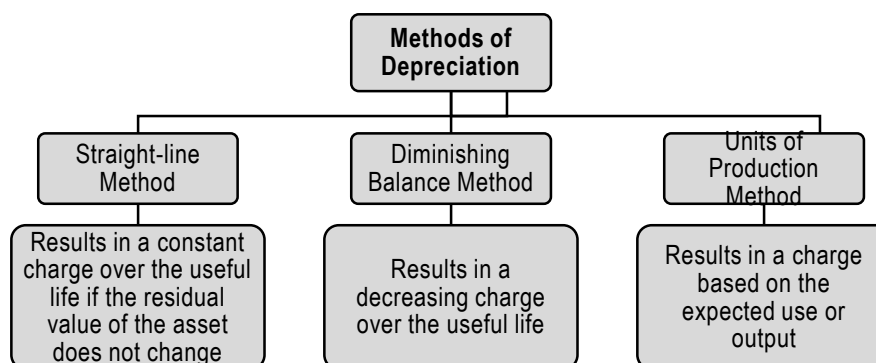
An increase in the value of the land on which a building stands does not affect the determination of the depreciable amount of the building.

**15. Depreciation Method**

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

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

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

**Review of Depreciation Method:**

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

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

**Depreciation Method based on Revenue:**

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

**16. Changes in Existing Decommissioning, Restoration and other Liabilities**

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

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

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

**17. Retirements**

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

- Carrying Amount, and
- Net Realisable Value

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

**18. De-recognition**

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

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

**19. Disclosure****General Disclosures:**

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

- (a) The measurement bases (i.e., cost model or revaluation model) used for determining the gross carrying amount;
- (b) The depreciation methods used;
- (c) The useful lives or the depreciation rates used.

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

- (d) The gross carrying amount and the accumulated depreciation (aggregated with accumulated impairment losses) at the beginning and end of the period; and
- (e) A reconciliation of the carrying amount at the beginning and end of the period showing:

**Additional Disclosures:**

The financial statements should also disclose:

- (a) The existence and amounts of restrictions on title, and property, plant and equipment pledged as security for liabilities;
- (b) The amount of expenditure recognised in the carrying amount of an item of property, plant and equipment in the course of its construction;
- (c) The amount of contractual commitments for the acquisition of property, plant and equipment;
- (d) If it is not disclosed separately on the face of the statement of profit and loss, the amount of compensation from third parties for items of property, plant and equipment that were impaired, lost or given up that is included in the statement of profit and loss; and
- (e) The amount of assets retired from active use and held for disposal.

**Disclosures related to Revalued Assets:**

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

- (a) The effective date of the revaluation;
- (b) Whether an independent valuer was involved;
- (c) The methods and significant assumptions applied in estimating fair values of the items;
- (d) The extent to which fair values of the items were determined directly by reference to observable prices in an active market or recent market transactions on arm's length terms or were estimated using other valuation techniques; and
- (e) The revaluation surplus, indicating the change for the period and any restrictions on the distribution of the balance to shareholders.



## 20. Transitional Provisions

### Previously Recognised Revenue Expenditure

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

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

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

### PPE acquired in Exchange of Assets

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

### Spare parts

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

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

### Revaluations

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

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

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

**PAPER – 2: BUSINESS LAW, ETHICS & COMMUNICATION**

**PART – I: ANNOUNCEMENTS STATING APPLICABILITY  
FOR MAY, 2018 EXAMINATIONS**

**Applicability for May, 2018 examinations**

The Study Material (July 2015 edition), Practice Manual (April 2016 edition) along with the “Supplementary Study Paper for November 2017 examinations and onwards” is relevant for May 2018 examinations. Supplementary Study Paper 2017 contains all relevant amendments/ circulars/ notifications etc. in the Business and the Company law part made from 1st May 2015 to 30th April, 2017. Further, all relevant amendments/ circulars/ notifications etc. in the Business Law and Company law part for the period 1st May 2017 to 31st October, 2017 are mentioned below:

<b>Relevant Legislative amendments from 1<sup>st</sup> of May 2017 to 31<sup>st</sup> of October 2017</b>				
<b>The Companies Act, 2013/ Corporate Laws</b>				
<b>Sl. No.</b>	<b>Amendments related to</b>	<b>Relevant Amendments</b>	<b>Page no. of the Study material (SM)/ Supplementary study paper (SSP) with reference of relevant provisions</b>	<b>Earlier Law</b>
1.	Exemptions to Government Companies Vide Notification G.S.R. 582(E) Dated 13th June, 2017	The Central Government amends the Notification G.S.R. 463(E), dated 5 <sup>th</sup> June 2015, whereby Exceptions, Modifications and Adaptations were provided in case of Government companies. Following is the amendments:  In sub-section (2) of section 96, for the words "such other place as the Central Government may approve in this behalf", the words "such other place within the city, town	Pg 6.128 of SM and Pg 12 of SSP.	Such other place as the Central Government may approve in this behalf.

		or village in which the registered office of the company is situate or such other place as the Central Government may approve in this behalf" shall be substituted.		
	Insertion of Paragraph 2A in the principal notification G.S.R. 463(E), dated 5 <sup>th</sup> June 2015	The aforesaid exceptions, modifications and adaptations (i.e. as given in Notification G.S.R. 463(E), dated 5 <sup>th</sup> June 2015 and Notification G.S.R. 582(E) Dated 13 <sup>th</sup> June, 2017) shall be applicable to a Government company which has not committed a default in filing of its financial statements under section 137 of the Companies Act or annual return under section 92 of the said Act with the Registrar.		
2.	Exemptions to Private Companies Vide Notification G.S.R. 583(E) Dated 13 <sup>th</sup> June, 2017	The Central Government amends the Notification G.S.R. 464(E), dated 5 <sup>th</sup> June 2015 whereby Exceptions, Modifications and Adaptations were provided in case of Private companies. Following are the amendments: (1) In Chapter V, clauses (a) to (e) of sub-section (2) of section 73, shall not apply to a private company- (A) which accepts from its members monies not exceeding one hundred per cent. of aggregate of the paid up share capital, free reserves and securities premium account; or (B) which is a start-up, for five years from the date of its incorporation; or	Pg 15 of SSP and 6.63 of SM	(1) Clause (a) to (e) of Section 73 provides conditions for acceptance of deposits from members. Notification dated 5 <sup>th</sup> June, 2015, provided that Clause (a) to (e) of Sub-section 2 of Section 73 shall not apply to private Companies which accepts from its members monies not exceeding one

		<p>(C) which fulfils all of the following conditions, namely:-</p> <p>(a) which is not an associate or a subsidiary company of any other company;</p> <p>(b) if the borrowings of such a company from banks or financial institutions or any body corporate is less than twice of its paid up share capital or fifty crore rupees, whichever is lower; and</p> <p>(c) such a company has not defaulted in the repayment of such borrowings subsisting at the time of accepting deposits under this section:</p> <p>Provided that the company referred to in clauses (A), (B) or (C) shall file the details of monies accepted to the Registrar in such manner as may be specified.</p> <p>(2) In Chapter VII, clause (g) of sub-section (1) of section 92, shall apply to private companies which are small companies, namely:-</p> <p>“(g) aggregate amount of remuneration drawn by directors;”</p>	Pg 6.124	<p>hundred per cent, of aggregate of the paid up share capital and free reserves, and such company shall file the details of monies so accepted to the Registrar in such manner as may be specified.</p> <p>(2) clause (g) of sub-section (1) of section 92 is read as “remuneration of directors and key managerial personnel”</p>
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		(3) In Chapter VII, proviso to sub-section (1) of section 92, For the proviso, the following proviso shall be substituted, namely:- “Provided that in relation to One Person Company, small company and private company (if such private company is a start-up), the annual return shall be signed by the company secretary, or where there is no company secretary, by the director of the company.”	Pg 6.125	(3) Whereas with respect to One Person Company and small company, the annual return shall be signed by the company secretary, or where there is no company secretary, by the director of the company.
	Insertion of Paragraph 2A in the principal notification G.S.R. 464(E), dated 5 <sup>th</sup> June 2015	The aforesaid exceptions, modifications and adaptations shall be applicable to a Private company which has not committed a default in filing of its financial statements under section 137 or annual return under section 92 of the said Act with the Registrar.		
3.	Vide notification S.O. 3086(E) dated 20th September 2017	The Central Government hereby appoints the 20th September, 2017 as the date on which proviso to clause (87) of section 2 of the said Act shall come into force.	Pg 6.8	Earlier not notified
<b>The Employees’ Provident Funds and Miscellaneous Provisions Act, 1952</b>				
4.	Amendments vide the Finance Act, 2017 (wef 26.5.2017)	The following amendments have been carried out in the Employees’ Provident Funds and Miscellaneous Provisions Act, 1952:  (1) in section 2, for clause (m), the following clause	-	(1) “Tribunal” means the Employees’

		<p>shall be substituted, namely: (m) "Tribunal" means the Industrial Tribunal referred to in section 7 D;</p> <p>(2) for section 7D, the following section shall be substituted, namely:- "7D. The Industrial Tribunal constituted by the Central Government under sub-section (1) of section 7A of the Industrial Disputes Act, 1947 shall, on and from the commencement of Part XIV of Chapter VI of the Finance Act, 2017, be the Tribunal for the purposes of this Act and the said Tribunal shall exercise the jurisdiction, powers and authority conferred on it by or under this Act."</p>	Pg 4.19	<p>Provident Funds Appellate Tribunal constituted under section 7D</p> <p>(2) <b>Employees' Provident Fund Appellate Tribunal (Section 7D):</b> The Central Government may, by notification in the Official Gazette, constitute one or more Appellate Tribunals to be known as the Employees' Provident Funds Appellate Tribunal to exercise the powers and discharge the functions conferred on such Tribunal by this Act and every such Tribunal shall have jurisdiction in respect of establishments situated in such area as may be specified in the notification constituting the Tribunal.</p> <p>A Tribunal shall consist of one person only to be appointed by the</p>
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		<p>(3) sections 7E, 7F, 7G and 7H shall be omitted</p>	Pg 4.19	<p>Central Government. A person shall not be qualified for appointment as the Presiding Officer of a Tribunal (hereinafter referred to as the Presiding Officer), unless he is, or has been, or is qualified to be a Judge of a High Court; or a District Judge.</p> <p>(3) The Study material contains only the citation of sections numbers 7E, 7F, 7G and 7H.</p>
		<p>(4) for section 18A, the following section shall be substituted, namely:— "18A. The authorities referred to in section 7A and every inspector shall be deemed to be a public servant within the meaning of section 21 of the Indian Penal Code."</p>	Pg 4.33	<p>(4) <b>Presiding Officer and other officers to be public servants (Section 18A):</b> The Presiding Officer of a Tribunal, its officers and other employees, the authorities referred to in Section 7-A and every inspector shall be deemed to be public servants within the meaning of Section 21 of the Indian Penal Code.</p>

## PART – II : QUESTIONS AND ANSWERS

## QUESTIONS

## PART – A: BUSINESS LAWS

## The Indian Contract Act, 1872

1. (a) Examine what is the legal position, as to the following:
    - (i) Ravi, Nalin and Ashok jointly borrowed ` 50,000 from Ajay. The whole amount was repaid to Ajay by Nalin. Decide in the light of the Indian Contract Act, 1872 whether:
      - (1) Nalin can recover the contribution from Ravi and Ashok,
      - (2) Legal representatives of Ravi are liable in case of death of Ravi,
      - (3) Nalin can recover the contribution from the assets, in case Ashok becomes insolvent.
    - (ii) Mr. MP entered into an agreement with Mr. ZX to deliver him (Mr. ZX) 5,000 bags to be manufactured in his factory. The bags could not be manufactured because of strike by the workers and Mr. MP failed to supply the said bags to Mr. ZX. Decide whether Mr. MP can be exempted from liability under the provisions of the Indian Contract Act, 1872.
  - (b) Shambhu becomes guarantor for Aman for the amount which may be given to him by Naveen within 6 months. The maximum limit of the said amount is ` 1 lakh. After two months Shambhu withdraws his guarantee. Up to the time of revocation of guarantee, Naveen had given to Aman ` 20,000.
    - (i) Whether Shambhu is discharged from his liabilities to Naveen for any subsequent loan.
    - (ii) Whether Shambhu is liable if Aman fails to pay the amount of ` 20,000 to Naveen?.
2. (a) Star gives to Sun a continuing guarantee to the extent of ` 15000 for the groceries to be supplied by Sun to Moon from time to time on credit. Afterwards, Moon became embarrassed, and without the knowledge of Star, Moon and Sun contract that Sun shall continue to supply Moon with groceries for ready money, and that the payments shall be applied to the then existing debts between Moon and Sun.

Examining the provision of the Indian Contract Act, 1872, decide whether Star is liable on his guarantee given to Sun.
  - (b) Shree hires a carriage of Jagdish and agrees to pay ₹ 500 as hire charges. The carriage is unsafe, though Jagdish is unaware of it. Shree is injured and claims



compensation for injuries suffered by her. Jagdish refuses to pay. Discuss the liability of Jagdish.

#### **The Negotiable Instruments Act, 1881**

3. A draws a bill on B. B accepts the bill without any consideration. The bill is transferred to C without consideration. C transferred it to D for value. Decide-
  - (i) Whether D can sue the prior parties of the bill, and
  - (ii) Whether the prior parties other than D have any right of action inter se?Give your answer in reference to the Provisions of Negotiable Instruments Act, 1881.
4. (a) What is a 'Sans Recours' endorsement? A bill of exchange is drawn payable to X or order. X endorses it to Y, Y to Z, Z to A, A to B and B to X. State with reasons whether X can recover the amount of the bill from Y, Z, A and B, if he has originally endorsed the bill to Y by adding the words 'Sans Recours'.
  - (b) A banker made payment of a cheque in which the drawers signature was forged. Can the banker claim protection in respect of such payment? What would be the protection if it was a case of forgery of endorsee's signature?

#### **The Payment of Bonus Act, 1965**

5. Mr. A, an employee of Earth Limited, retired from the company on 31<sup>st</sup> March, 2017 and died after few months. Y, the heir of Mr. A, applied within the prescribed time to the company for payment of bonus of Mr. A which was due for the year ending 31<sup>st</sup> March, 2017. The company refused to pay the bonus. Examine the validity of the company's refusal and also state the procedure to recover the bonus under the provisions of the Payment of Bonus Act, 1965.
6. In 2009, the Tele Corporation, a Public Sector establishment under the Department of Science and Technology, Government of Rajasthan starts to sell mobile sets manufactured by it, in addition to T.V. sets, so as to compete with private sector establishments of mobile sets in the market. The income from sale of mobile sets is 30 percent of the gross income of the Corporation. The employees of the Corporation went to strike for demand of Bonus. Decide, whether the demand of the employees is tenable under the provisions of the Payment of Bonus Act, 1965. Would your answer be different if the income from sale of mobile sets is only 10 percent of the gross income of the Corporation?

#### **The Employees' Provident Funds and Miscellaneous Provisions Act, 1952**

7. Mr. Avinash, an employee working in an establishment covered by the Employees' Provident Funds and Miscellaneous Provisions Act, 1952, leaves his employment and takes up employment in another establishment. State in this connection:
  - (i) How shall the amount accumulated to his Provident Fund Account be transferred?

- (ii) What steps shall be taken if the establishment in which he has joined is not covered by the Act?
  - (iii) What would be your answer if the establishment in which he was previously working is not covered by the Act?
8. Satinder retired from the services of PQR Limited, on 31st March, 2016. He had a sum of ₹ 5 lac in his Provident Fund Account. It has become due for payment to Satinder on 30<sup>th</sup> April, 2016 but the company made the payment of the said amount after one year. Satinder claimed for the payment of interest on due amount at the rate of 15 percent per-annum for one year. Decide, whether the claim of Satinder is tenable under the provisions of the Employees' Provident Funds and Miscellaneous Provisions Act, 1952.

#### **The Payment of Gratuity Act, 1972**

9. Mr. Naresh was an employee of LMO Limited. He retired from the company after completing 30 years of continuous service. He applied to the company for the payment of gratuity within the prescribed time. The company refused to pay the gratuity and contended that due to stringent financial condition the company is unable to pay the gratuity. Mr. Naresh applied to the Appropriate Authority for the recovery of the amount of gratuity.
- Examine the validity of the contention of the company and also state the provisions of law to recover the gratuity under the Payment of Gratuity Act, 1972.
10. Mr. Kartik is employed in Akshara Limited, a seasonal establishment. The factory was in operation from 1st March to 30th June during the financial year 2015-16. Though, Mr. Kartik was not in continuous service during this period, he had worked for 95 days. Referring to the provisions of the Payment of Gratuity Act, 1972, decide whether Mr. Kartik is entitled to gratuity.

#### **The Companies Act, 2013**

11. Exceptional Builders Limited decides to pay 2.5 percent of the value of debentures as underwriting commission to the underwriters but the Articles of the company authorize only 2.0 percent underwriting commission on debentures. The company further decides to pay the underwriting commission in the form of flats. Examine the validity of the above arrangements under the provisions of the Companies Act, 2013.
12. (a) In a General Meeting of Amit Limited, the Chairman directed to exclude certain matters detrimental to the interest of the company from the minutes. Manoj, a shareholder contended that the minutes must contain fair and correct summary of the proceedings thereat. Decide, whether the contention of Manoj is maintainable under the provisions of the Companies Act, 2013?
- (b) Misha India Ltd. owed to Sunil ₹1,000. On becoming this debt payable, the company offered Sunil 10 shares of ₹100 each in full settlement of the debt. The said shares were fully paid and were allotted to Sunil.

Examine the validity of these allotments in the light of the provisions of the Companies Act, 2013.

13. The paid-up share capital of Saras Private Limited is ` 1 crore, consisting of 8 lacs Equity Shares of ` 10 each, fully paid-up and 2 lacs Cumulative Preference Shares of `10 each, fully paid-up. Jeevan Private Limited and Sudhir Private Limited are holding 3 lacs Equity Shares and 50,000 Equity Shares respectively in Saras Private Limited. Jeevan Private Limited and Sudhir Private Limited are the subsidiaries of Piyush (PQR) Private Limited. With reference to the provisions of the Companies Act, 2013 examine whether Saras Private Limited is a subsidiary of Piyush Private Limited? Would your answer be different if Piyush Private Limited has 8 out of 9 Directors on the Board of Saras Private Limited?
14. Zenab Limited held its Annual General Meeting on September 15, 2016. The meeting was presided over by Mr. Venkat, the Chairman of the Company's Board of Directors. On September 17, 2016, Mr. Venkat, the Chairman, without signing the minutes of the meeting, left India to look after his father who fell sick in London. Referring to the provisions of the Companies Act, 2013, state the manner in which the minutes of the above meeting are to be signed in the absence of Mr. Venkat and by whom.
15. Zorab Limited served a notice of General Meeting upon its members. The notice stated that a resolution to increase the share capital of the Company would be considered at such meeting. A shareholder complained that the amount of the proposed increase was not specified in the notice. Is the notice valid?

**PART – B: ETHICS**

16. State, how far a sound ethical environment in a company may be created and corporate scandals may be avoided.
17. What do you understand by the term "Acid Rain"? How does it adversely affect the environment?
18. What reasons force a marketing executive to adopt ethical practices in marketing? Explain.
19. Explain the role played by different committees in regulating the 'Corporate Governance'.
20. State the elements which create discrimination in employment in the business organizations.

**PART – C: COMMUNICATION**

21. What is an Indemnity Bond? Supply a format for Indemnity Bond.
22. Write Short notes on:
  - (a) Guidelines for drafting a Pres Release
  - (b) The Press Communiqué.
23. Explain the key elements involved in the innovation frame work of an organisation.
24. What do you understand by "ethical communication"? What are its elements.

25. Discuss personal competencies that are associated with Emotional Intelligence.

### SUGGESTED ANSWERS/HINTS

1. (a) (i) Section 42 of the Indian Contract Act, 1872 requires that when two or more persons have made a joint promise, then, unless a contrary intention appears from the contract, all such persons jointly must fulfill the promise. In the event of the death of any of them, his representative jointly with the survivors and in case of the death of all promisors, the representatives of all jointly must fulfill the promise.

Section 43 allows the promisee to seek performance from any of the joint promisors. The liability of the joint promisors has thus been made not only joint but "joint and several". Section 43 provides that in the absence of express agreement to the contrary, the promisee may compel any one or more of the joint promisors to perform the whole of the promise.

Section 43 deals with the contribution among joint promisors. The promisors, may compel every joint promisor to contribute equally to the performance of the promise (unless a contrary intention appears from the contract). If any one of the joint promisors makes default in such contribution the remaining joint promisors must bear the loss arising from such default in equal shares.

As per the provisions of above sections,

- (1) Nalin can recover the contribution from Ravi and Ashok because Ravi, Nalin and Ashok are joint promisors.
  - (2) Legal representative of Ravi are liable to pay the contribution to Nalin. However, a legal representative is liable only to the extent of property of the deceased received by him.
  - (3) Nalin also can recover the contribution from Ashok's assets.
- (ii) According to Section 56 of the Indian Contract Act, 1872 when the performance of a contract becomes impossible or unlawful subsequent to its formation, the contract becomes void, this is termed as 'supervening impossibility' (i.e. impossibility which does not exist at the time of making the contract, but which arises subsequently).

But impossibility of performance is, as a rule, not an excuse from performance. It means that when a person has promised to do something, he must perform his promise unless the performance becomes absolutely impossible. Whether a promise becomes absolutely impossible depends upon the facts of each case.

The performance does not become absolutely impossible on account of strikes, lockout and civil disturbances and the contract in such a case is not discharged

unless otherwise agreed by the parties to the contract (*Budget V Bennington; Jacobs V Credit Lyonnais*).

In this case Mr. MP could not deliver the bags as promised because of strike by the workers. This difficulty in performance cannot be considered as impossible of performance attracting Section 56 and hence Mr. MP is liable to Mr. ZX for non-performance of contract.

- (b) As per section 130 of the India Contract Act, 1872, a continuing guarantee may, at any time, be revoked by the surety, as to future transactions, by notice to the creditor, but the surety remains liable for transactions already entered into. Thus, a specific guarantee cannot be revoked by the surety if the liability has already accrued.
- (i) In the given situation, Shambhu is discharged from all the subsequent loans because it's a case of continuing guarantee.
- (ii) Shambhu is liable for payment of ` 20,000 to Naveen because the transaction has already completed.
2. (a) The problem as asked in the question is based on the provisions of the Indian Contract Act, 1872 as contained in Section 133. The section provides that any variance made without the surety's consent in the terms of the contract between the principal debtor and the creditor, discharges the surety as to transactions subsequent to the variance.

In the given problem all the above requirements are fulfilled. Therefore, Star is not liable on his guarantee for the vegetable supplied after this new arrangements. The reason for such a discharge is that the surety agreed to be liable for a contract which is no more there and he is not liable on the altered contract because it is different from the contract made by him.

- (b) Problem asked in the question is based on the provisions of the Indian Contract Act, 1872 as contained in Section 150. The section provides that if the goods are bailed for hire, the bailor is responsible for such damage, whether he was or was not aware of the existence of such faults in the goods bailed.

Accordingly, applying the above provisions in the given case Jagdish is responsible to compensate Shree for the injuries sustained even if he was not aware of the defect in the carriage.

3. 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 given situation, Arun has drawn a bill on Barun and Barun accepted the bill without consideration and transferred it to Tarun without consideration. Later on in the next transfer by Tarun to Deep is for value. According to provisions of the aforesaid section 43, the bill ultimately has been transferred to Deep with consideration. Therefore, Deep can sue any of the parties i.e. Arun, Barun or Tarun, as Deep arrived a good title on it being taken with consideration.
- (ii) As regards to the second part of the problem, the prior parties before Deep i.e., Arun, Barun, and Tarun have no right of action inter se because first part of Section 43 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.

4. (a) **Meaning of Sans Recours Endorsement:** It is a type of endorsement on a Negotiable Instrument by which the endorser absolves himself or declines to accept any liability on the instrument of any subsequent party. The endorser signs the endorsement putting his-signature along with the words, "SANS RECOURS".

In the problem X, the endorser becomes the holder after it is negotiated to several parties. Normally, in such a case, none of the intermediate parties is liable to X. This is to prevent 'circuitry of action'. But in this case X's original endorsement is 'sans recours' and therefore, he is not liable to Y, Z, A and B. But if the bill is negotiated back to X, all of them are liable to him and he can recover the amount from all or any of them.

- (b) In case of cheques, the paying banker is given statutory protection against the payment of cheques having forged endorsements. And the banker cannot be held liable if it makes payment in good faith and without any negligence (Section 85, the Negotiable Instruments Act, 1881). But the banker will not be protected where the payment of a cheque is made on which the drawer's signature was forged. The reason for the same is that the banker is protected only in case of forgery of endorser's signature and not in case of forgery of drawer's signature.
5. According to section 19 of the Payment of Bonus Act, 1965 the employer is bound to pay in cash the bonus payable to an employee within eight months from the close of the accounting year.

In the present case, the bonus should be paid by 30<sup>th</sup> November 2017.

Hence, company's refusal to not pay the bonus is not valid under the Act.

The remedy available to Y the heir of Mr. A lies in section 21 of the Payment of Bonus Act under which an employee, his assignee or his heirs, can make an application for the recovery of the amount to the Appropriate Government within one year from the date on which the bonus becomes due. If the appropriate government or the prescribed authority is satisfied that any money is so due, it shall issue a certificate for that amount to the

Collector who shall proceed to recover the same in the same manner as an arrear of land revenue.

6. Section 20(1) of the Payment of Bonus Act, 1956 provides that, if in any accounting year, an establishment in public sector sells any goods produced or manufactured by it or if it renders any services in competition with an establishment in private sector and if the income from such sale or service or both is not less than 20% of the gross income of such establishment, then the provisions of the Payment of Bonus Act, 1956 shall apply in relation to establishment in private Sector.

In terms of section 20(2), the provisions of the Payment of Bonus Act, 1965 do not apply to an establishment in public sectors, except as provided under sub section 1 of section 20.

Thus, in the given situation since the income from sale of mobile sets is 30% (i.e. more than 20%) of the gross income of the Corporation, the demand of employees is tenable.

However, in the second case, as the income from sale of mobile sets is 10% (i.e. less than 20%) of the gross income of the Corporation, the demand of employees is not tenable.

7. **Transfer of accumulated amount to the credit of Employees' Provident Funds on change of employment**

Section 17 A (1) provides that where an employee employed in an establishment to which this Act applies leaves his employment and obtains re-employment in another establishment to which this Act does not apply, the amount of accumulations to the credit of such employee in the provident fund of the establishment left by him shall be transferred, within such time as may be specified by the Central Government in this behalf, to the credit of his account in the provident fund of the establishment in which he is re-employed, if the employee so desires and the rules in relation to that provident fund permit such transfer.

Similarly, under sub section (2) where an employee employed in an establishment to which this Act does not apply leaves his employment and obtains re-employment in another establishment to which this Act applies, the amount of accumulations to the credit of such employee in the provident fund of the establishment left by him may, if the employee so desires and the rules in relation to such provident fund permit, be transferred to the credit of his account in the Fund or as the case may be, in the provident fund of the establishment in which he is re-employed.

8. According to Section 7Q of the Employees' Provident Funds and Miscellaneous Provisions Act, 1952 the employer shall be liable to pay simple interest @ of 12% per annum or at such higher rate as may be specified in the Scheme on any amount due from him under this Act from the date on which the amount has become so due till the date of its actual payment:

Provided that higher rate of interest specified in the Scheme shall not exceed the lending rate of interest charged by any scheduled bank.

As per above provision, Satinder can claim for the payment of interest on due amount @ 12 percent per annum or at the rate specified in the Scheme, whichever is higher, for one year. Here, in the absence of specified rate, Satinder can claim only 12 percent per annum interest on the due amount.

Hence, claim of Satinder for interest rate of 15% is not tenable.

9. (1) Gratuity shall be payable to an employee on the termination of his employment after he has rendered continuous service for not less than five years on his superannuation or on his retirement or resignation or on his death or disablement due to accident or disease under Section 4(1) of the Payment of Gratuity Act, 1972. Further, section 7(2) provides that as soon as gratuity becomes payable, the employer shall, whether the application for the payment of gratuity has been given or not by the employee, determine the amount of gratuity and give notice in writing to the person to whom the gratuity is payable and also to the controlling authority specifying the amount of gratuity so determined.

The employer shall arrange to pay the amount of gratuity within 30 days for the date of its becoming due/payable to the person to whom it is payable [Section 7(3)], along with simple interest (at rates specified) if it is not paid within the period specified except where the delay in the payment is due to the fault of the employee and the employer has obtained permission thereon from the Controlling Authority [Section 7(3A)].

- (2) If the gratuity payable under the Act is not paid by the employer within the prescribed time to the person entitled thereto, the Controlling Authority shall issue a certificate for the amount to the Collector to recover the same along with compound interest at such rate as prescribed by the Central Government from the date of expiry of the prescribed time as land revenue arrears, to enable the person entitled to get the amount, after receiving the application from the aggrieved person (Section 8).

Before issuing the certificate for such recovery the Controlling Authority shall give the employer a reasonable opportunity of showing cause against the issue of such certificate. The amount of interest payable under the Section shall not exceed the amount of gratuity payable under this Act in no case (Section 8).

In the given case the facts are commensurate with provisions of law as stated above under Sections 7 and 8 of the Payment of Gratuity Act, 1972. Therefore, Mr. Naresh is entitled to recover gratuity as he has completed the service of 30 years. The company cannot take the plea of stringent financial conditions for not paying the gratuity to Mr. Naresh. On the refusal by the company, Mr. Naresh can apply to the appropriate authority and the company will be liable to pay the gratuity along with interest as decided by such authority.

10. According to sub-section 3 of Section 2A of the Payment of Gratuity Act, 1972 provides that where an employee, employed in a seasonal establishment, is not in continuous service within the meaning of clause (1), for any period of one year or six months, he shall



be deemed to be in continuous service under the employer for such period if he has actually worked for not less than seventy-five percent of the number of days on which the establishment was in operation during such period.

In the given problem, Mr. Kartik has worked for 95 days in Akshara Limited, and as per the above provision, Mr. Kartik has worked for more than 75 % of number of days on which the establishment was in operation i.e. 75 % of 120 days (1st of March to 30th June) = 90 days. Therefore, Mr. Kartik shall be entitled for gratuity.

11. Section 40 (6) of the Companies Act 2013, provides that a company may pay commission to any person in connection with the subscription or procurement of subscription to its securities, whether absolute or conditional, subject to the a number of conditions which are prescribed under *Companies (Prospectus and Allotment of Securities) Rules, 2014*. In relation to the case given, the conditions applicable under the above Rules are as under:
- (a) The payment of such commission shall be authorized in the company's articles of association;
  - (b) The commission may be paid out of proceeds of the issue or the profit of the company or both;
  - (c) The rate of commission paid or agreed to be paid shall not exceed, in case of shares, five percent (5%) of the price at which the shares are issued or a rate authorised by the articles, whichever is less, and in case of debentures, shall not exceed two and a half per cent (2.5 %) of the price at which the debentures are issued, or as specified in the company's articles, whichever is less;

Thus, the Underwriting commission is limited to 5% of issue price in case of shares and 2.5% in case of debentures. The rates of commission given above are maximum rates.

In view of the above, the decision of Exceptional Builders Ltd. to pay underwriting commission exceeding 2% as prescribed in the Articles is invalid.

The company may pay the underwriting commission in the form of flats as both the Companies Act and the Rules do not impose any restriction on the mode of payment though the source has been restricted to either the proceeds of the issue or profits of the company.

12. (a) Under Section 118 (5) of the Companies Act, 2013, there shall not be included in the Minutes of a meeting, any matter which, in the opinion of the Chairman of the meeting:
- (i) is or could reasonably be regarded as defamatory of any person;
  - (ii) is irrelevant or immaterial to the proceeding; or
  - (iii) is detrimental to the interests of the company;

Further, under section 118(6) the chairman shall exercise absolute discretion in regard to the inclusion or non-inclusion of any matter in the Minutes on the grounds specified in sub-section (5) above.

Hence, in view of the above, the contention of Manoj, a shareholder of Amit Limited is not valid because the Chairman has absolute discretion on the inclusion or exclusion of any matter in the minutes for aforesaid reasons.

- (b) Under section 62 (1) (c) of the Companies Act, 2013 where at any time, a company having a share capital proposes to increase its subscribed capital by the issue of further shares, either for cash or for a consideration other than cash, such shares may be offered to any persons, if it is authorised by a special resolution and if the price of such shares is determined by the valuation report of a registered valuer subject to such conditions as may be prescribed.

In the present case, Misha India Ltd is empowered to allot the shares to Sunil in settlement of its debt to him. The issue will be classified as issue for consideration other than cash and thus must be approved by the members by a special resolution. Further, the valuation of the shares must be done by a registered valuer.

13. In terms of section 2 (87) of the Companies Act 2013 "subsidiary company" or "subsidiary", in relation to any other company (that is to say the holding company), means a company in which the holding company—

- (i) controls the composition of the Board of Directors; or
- (ii) exercises or controls more than one-half of the total share capital either at its own or together with one or more of its subsidiary companies:

Provided that such class or classes of holding companies as may be prescribed shall not have layers of subsidiaries beyond such numbers as may be prescribed.

Explanation.—For the purposes of this clause,—

- (a) a company shall be deemed to be a subsidiary company of the holding company even if the control referred to in sub-clause (i) or sub-clause (ii) is of another subsidiary company of the holding company;
- (b) the composition of a company's Board of Directors shall be deemed to be controlled by another company if that other company by exercise of some power exercisable by it at its discretion can appoint or remove all or a majority of the directors.

In the present case, Jeevan Pvt. Ltd. and Sudhir Pvt. Ltd. together hold less than one half of the total share capital. Hence, Piyush Private Ltd. (holding of Jeevan Pvt. Ltd. and Sudhir Pvt) will not be a holding company of Saras Pvt. Ltd.

However, if Piyush Pvt. Ltd. has 8 out of 9 Directors on the Board of Saras Pvt. Ltd. i.e. controls the composition of the Board of Directors; it (Piyush Pvt. Ltd.) will be treated as the holding company of Saras Pvt. Ltd.

14. Section 118 of the Companies Act, 2013 provides that every company shall prepare, sign and keep minutes of proceedings of every general meeting, including the meeting called by the requisitionists and all proceedings of meeting of any class of shareholders or

creditors or Board of Directors or committee of the Board and also resolution passed by postal ballot within thirty days of the conclusion of every such meeting concerned. Minutes kept shall be evidence of the proceedings recorded in a meeting.

By virtue of Rule 25 of the Companies (Management and Administration) Rules 2014 read with section 118 of the Companies Act, 2013 each page of every such book shall be initialled or signed and the last page of the record of proceedings of each meeting or each report in such books shall be dated and signed by, in the case of minutes of proceedings of a general meeting, by the chairman of the same meeting within the aforesaid period of thirty days or in the event of the death or inability of that chairman within that period, by a director duly authorized by the Board for the purpose.

Therefore, the minutes of the meeting referred to in the case given above can be signed in the absence of Mr Venkat, by any director who is authorized by the Board.

15. Under section 102(2)(b) in the case of any meeting other than an AGM, all business transacted thereat shall be deemed to be special business.

Further under section 102 (1), a statement setting out the following material facts concerning each item of special business to be transacted at a general meeting, shall be annexed to the notice calling such meeting, namely:—

- (a) the nature of concern or interest, financial or otherwise, if any, in respect of each items, of:
  - (i) every director and the manager, if any;
  - (ii) every other key managerial personnel; and
  - (iii) relatives of the persons mentioned in sub-clauses (i) and (ii);
- (b) any other information and facts that may enable members to understand the meaning, scope and implications of the items of business and to take decision thereon.

Thus, the objection of the shareholder is valid since the details on the item to be considered are lacking. The information about the amount is a material fact with reference to the proposed increase of share capital. The notice is, therefore, not a valid notice under Section 102 of the Companies Act, 2013.

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

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

Some ethical organisations are having policies to train and motivate employees towards ethical behaviour. To start with, such initiation should be from the top. A number of companies in India and abroad are being known for their quality and soundness of their ethics programmes.

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

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

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

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

17. Acid Rain” is a threat to the environment that is closely related to the combustion of fossil fuels (oil, coal and natural gases) which are heavily used by utilities to produce electricity. Burning fossil fuels, particularly coal containing high levels of sulphur, releases large quantities of sulphur oxides and nitrogen oxides into the atmosphere. When these gases are carried into the air, they combine with water vapour in clouds to form nitric acid and sulphuric acid. These acids are then carried down in rain, which often falls hundreds of miles away from the original sources of the oxides raising the acidity of the water sources. It also soaks into soils and falls directly on trees and other vegetations.

Numerous studies have shown that many fish populations and other aquatic organisms are unable to survive in lakes and rivers that have become highly acidic due to acid rain. Other studies have shown that acid rain directly damages forests and indirectly destroys the wildlife and species that depend on forests for food and breeding. Acidic rain water can also contaminate drinking water. Acid rain can corrode and damage buildings, statues and other objects, particularly those made of iron, lime stone and marble thereby causing great threat to life and property over a long period of time.

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

1. **To reverse declining public confidence in marketing:** Sometime misleading package labels, false claim in advertisement, phony list prices, infringement of trademarks pervert the market trends and such behaviour damages the marketers' reputation. To reverse this situation, business leaders must demonstrate convincingly that they are aware of their ethical responsibility and will fulfill it. Companies must set high ethical standards and enforce them. Moreover, it is in management's interest to be concerned with the well- being of consumers, since they are the lifeblood of a business.
2. **To avoid increase in government regulation:** Business apathy, resistance, or token responses to unethical behaviour increase the probability of more governmental regulation. The governmental limitations may also result from management's failure

to live up to its ethical responsibilities. Moreover, once the government control is introduced, it is rarely removed.

3. **To retain power granted by society:** Marketing executives wield a great deal of social power as they influence markets and speak out on economic issues. However, there is a responsibility tied to that power. If marketers do not use their power in a socially acceptable manner, that power will be lost in the long run.
4. **To protect the image of the organisation:** Buyers often form an impression of an entire organisation based on their contact with one person. That person represents the marketing function. Sometimes a single sales clerk may pervert the market opinion in relation to that company which he represents.

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

19. **Role of different committees in regulating corporate governance:** The core roles of the various committees in regulation of corporate governance are as follows:
  1. **Board of Directors:** The Board's role is that of trusteeship to protect and enhance shareholders value through strategic supervision. The strategy should aim at accountability and fulfillment of goals.
  2. **Audit Committee:** They have to provide assurance to Board on adequacy of internal control systems and financial disclosures.
  3. **Compensation Committee:** The committee has to recommend to the Board compensation terms for executive Directors and the senior most level of management below the Executive Directors.
  4. **Nomination Committee:** It is to recommend to the Board nominations for membership of the Corporate Management Committee and the Board, and oversee succession to the senior most level of management below the Executive Directors.
  5. **Investor Services Committee:** It is to look into redressal of Shareholders' and Investors' grievances, approval of transmissions, sub-division of shares, issue of duplicate shares etc.
  6. **Corporate Management Committee:** Its primary role is strategic management of company's businesses within Board's approved direction/framework.
  7. **Divisional Management Committee:** It is to realize tactical and strategic objectives in accordance with Corporate Management Committee/Board approved plan.
20. 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.

## 21. Indemnity Bond

A contract of indemnity as defined under Section 124 of the Indian Contract Act, 1872 is a contract by which one party promises to save the other from loss caused to him by the contract of the promissory himself, or by the contract of any other person. A person who gives the indemnity is called indemnifier and a person for whom protection is given is called the indemnity holder. The model form of indemnity bond is given below:

Name of the Assessee:

P.A.N. No..... Assessment Year:.....

I ..... son/ wife/ daughter of ..... Resident of ..... do hereby agree to indemnify the Government of India for any loss that may occur on giving credit for the Certified Photostat copies of the TDS Certificates/ ...../...../ ..... for a sum of ₹..... being ... % of my share in the total TDS of ₹ ..... of ..... I further declare that the credit for consolidated TDS Certificate was not claimed in the hands of the Association of Persons,.....

Date:

Signature:

Place:

22. (a) **Guidelines for drafting a Press Release:** The term press release in its narrower sense is used for releases covering news. The press release contains worthwhile material which has some news value.

The press release should be written in a journalistic style. It should provide facts or information of interest to the readers and should attempt to cover all aspects of a specific subject. There should not be any loose ends. It should be on a subject which is recent or in news. The release should not be generally lengthy. It should be concise and to the point. It has not much place for subsidiary or background material.

The introduction or lead should be in a summary format as it is a news story.

The releases should have a consistent format. Generally, the name of the organization from where the release emanates is given on the top. The date and place are indicated on the top right side. The release should have a title and a sub-title also, if necessary. It should have a suitable introductory paragraph. In the case of releases from non-official organization, it is desirable also to mention the designation of the person issuing the release and his telephone number.

- (b) **The Press Communiqué:** The press communiqués are issued when some important government decisions or announcements are made such as cabinet appointments, conclusion of the foreign dignitaries' visits, international agreement, etc. The press communiqué is formal in character. It carries the name of the ministry or department and the place, the date at the bottom left-hand corner of the release. Generally, the press is expected to reproduce the press communiqué without any substantial change. No heading or subheading is given on press communiqués.

23. **The key elements in the innovation framework are:**

- (i) **Accessibility:** The major organizational challenge is to make everyone, particularly the workers as active participants in the work process. The innovative enterprise ensures everyone is accessible to each other at all levels within the organization.
- (ii) **Recognize and reward innovation:** One of the more radical steps an organization or manager can take is to make innovation a requirement of the job.
- (iii) **Develop company programs that encourage innovation:** Some companies allow their employees to take sabbaticals to work in a new environment or teach in a college. By placing employees in different environments, they can meet new people, come across new ideas and hopefully generate their own novel approaches.
- (iv) **Foster informal communication:** The paperwork involved in proposing or even pursuing a project can be a major roadblock to innovation. Employees often feel stifled when asked to fully justify ideas; they may be working on a hunch.

- (v) **Information:** The right kind of information is called information. This type of information is critical to the vitality of the enterprises. Information consists of the plans, vision, goals and all the new ideas affecting the enterprises. The innovative enterprise is looking forward continuously changing and adapting to the needs of the customer.
- (vi) **Framework:** The innovative enterprise must constantly adapt, create and innovate. Information and communication are the wind that sails the innovative enterprise towards its destination. Information and communication pose difficult challenges for most businesses. The difficulty lies in balancing the flow of information between providing too much or too little information.

24. According to the National communication Association, ethical communication is fundamental to responsible thinking, decision making and the development of relationship and communities within and across contexts, cultures, channels and media. Ethical communication enhances human worth and dignity by fostering, truthfulness, fairness, responsibility, personal integrity and respect for self and others'. While unethical communication threatens the quality of all communication and consequently the well-being of individuals and the society in which we live. In nutshell ethical communicators have a 'well developed sense of social responsibility'.

An ethical communication is one which:

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

25. **Emotional Intelligence:** Emotional intelligence refers to the capacity to recognizing your own feelings and those of others, for motivating yourself, and for managing emotions well in yourself and in your relationships.

Personal competencies associated with emotional intelligence are as follows:

Self-Awareness

- *Emotional self-awareness:* Reading your own emotions and recognizing their impact; using 'gut sense' to guide decisions



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

**PAPER – 3: COST ACCOUNTING AND FINANCIAL MANAGEMENT**

**PART-I: COST ACCOUNTING**

**QUESTIONS**

**Material**

1. Banerjee Brothers (BB) supplies surgical gloves to nursing homes and polyclinics in the city. These surgical gloves are sold in pack of 10 pairs at price of ₹ 250 per pack.

For the month of April 2018, it has been anticipated that a demand for 60,000 packs of surgical gloves will arise. BB purchases these gloves from the manufacturer at ₹ 228 per pack within a 4 to 6 days' lead time. The ordering and related cost is ₹ 240 per order. The storage cost is 10% p.a. of average inventory investment.

Required:

- (i) Calculate the Economic Order Quantity (EOQ)
- (ii) Calculate the number of orders needed every year
- (iii) Calculate the total cost of ordering and storage of the surgical gloves.
- (iv) Determine when should the next order to be placed. (Assuming that the company does maintain a safety stock and that the present inventory level is 10,033 packs with a year of 360 working days).

**Labour**

2. Sonali Ltd. wants to ascertain the profit lost during the year 2017-18 due to increased labour turnover. For this purpose, it has 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 2017-18.

**Overheads**

3. World Class Manufacturers – a small scale enterprise, produces a single product and has adopted a policy to recover the production overheads of the factory by adopting a single blanket rate based on machine hours. The annual budgeted production overheads for the year 2017-18 are ₹ 44,00,000 and budgeted annual machine hours are 2,20,000.

For a period of first six months of the financial year 2017-18, following information were extracted from the books:

Actual production overheads	₹ 24,88,200
Amount included in the production overheads:	
Paid as per court's order	₹ 1,28,000
Expenses of previous year booked in current year	₹ 1,200
Paid to workers for strike period under an award	₹ 44,000
Obsolete stores written off	₹ 6,700

Production and sales data of the concern for the first six months are as under:

Production:	
Finished goods	24,000 units
Works-in-progress (50% complete in every respect)	18,000 units
Sale:	
Finished goods	21,600 units

The actual machine hours worked during the period were 1,16,000 hours. It is revealed from the analysis of information that  $\frac{1}{4}$  of the under/ over absorption was due to defective production policies and the balance was attributable to increase/decrease in costs.

**Required:**

- Determine the amount of under/over absorption of production overheads for the six-month period of 2017-18.
- Show the accounting treatment of under/ over absorption of production overheads, and
- Apportion the under/ over absorbed overheads over the items.

**Non-Integrated Accounts**

4. As of 31st March, 2018, the following balances existed in a firm's cost ledger, which is maintained separately on a double entry basis:

	Debit (₹)	Credit (₹)
Stores Ledger Control A/c	3,20,000	—

Work-in-process Control A/c	1,52,000	–
Finished Goods Control A/c	2,56,000	–
Manufacturing Overhead Control A/c	–	28,000
Cost Ledger Control A/c	–	7,00,000
	7,28,000	7,28,000

During the next quarter, the following items arose:

	(₹)
Finished Product (at cost)	2,35,500
Manufacturing overhead incurred	91,000
Raw material purchased	1,36,000
Factory wages	48,000
Indirect labour	20,600
Cost of sales	1,68,000
Materials issued to production	1,26,000
Sales returned (at cost)	8,000
Materials returned to suppliers	11,000
Manufacturing overhead charged to production	86,000

You are required to prepare the Cost Ledger Control A/c, Stores Ledger Control A/c, Work-in-process Control A/c, Finished Stock Ledger Control A/c, Manufacturing Overhead Control A/c, Wages Control A/c, Cost of Sales A/c and the Trial Balance at the end of the quarter as per costing records.

### Batch Costing

5. Arnav Confectioners (AC) owns a bakery which is used to make bakery items like pastries, cakes and muffins. AC use to bake atleast 50 units of any item at a time. A customer has given an order for 600 cakes. To process a batch, the following cost would be incurred:

Direct materials - ₹ 5,000

Direct wages - ₹ 500 (irrespective of units)

Oven set-up cost - ₹750 (irrespective of units)

AC absorbs production overheads at a rate of 20% of direct wages cost. 10% is added to the total production cost of each batch to allow for selling, distribution and administration overheads.

AC requires a profit margin of 25% of sales value.

**Required:**

- (i) Determine the price to be charged for 600 cakes.
- (ii) Calculate cost and selling price per cake.
- (iii) What would be selling price per unit If the order is for 605 cakes.

**Process Costing**

6. Akash Ltd. manufactures chemical solutions for the food processing industry. The manufacturing takes place in a number of processes and the company uses FIFO method to value work-in-process and finished goods. At the end of the last month, a fire occurred in the factory and destroyed some of paper containing records of the process operations for the month.

Akash Ltd. needs your help to prepare the process accounts for the month during which the fire occurred. You have been able to gather some information about the month's operating activities but some of the information could not be retrieved due to the damage. The following information was salvaged:

- Opening work-in-process at the beginning of the month was 800 litres, 70% complete for labour and 60% complete for overheads. Opening work-in-process was valued at ₹ 26,640.
- Closing work-in-process at the end of the month was 160 litres, 30% complete for labour and 20% complete for overheads.
- Normal loss is 10% of input and total losses during the month were 1,800 litres partly due to the fire damage.
- Output sent to finished goods warehouse was 4,200 litres.
- Losses have a scrap value of ₹15 per litre.
- All raw materials are added at the commencement of the process.
- The cost per equivalent unit (litre) is ₹39 for the month made up as follows:

	(₹)
Raw Material	23
Labour	7
Overheads	9
	39

**Required:**

- (a) Calculate the quantity (in litres) of raw material inputs during the month.
- (b) Calculate the quantity (in litres) of normal loss expected from the process and the quantity (in litres) of abnormal loss / gain experienced in the month.

- (c) Calculate the values of raw material, labour and overheads added to the process during the month.
- (d) Prepare the process account for the month.

### Joint Products & 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

### Standard Costing

8. Shyamali Ltd. had prepared the following estimation for the month of April:

	Quantity	Rate (₹)	Amount (₹)
Material-A	800 kg.	45.00	36,000
Material-B	600 kg.	30.00	18,000
Skilled labour	1,000 hours	37.50	37,500
Unskilled labour	800 hours	22.00	17,600

Normal loss was expected to be 10% of total input materials and an idle labour time of 5% of expected labour hours was also estimated.

At the end of the month the following information has been collected from the cost accounting department:

The company has produced 1,480 kg. finished product by using the followings:

	Quantity	Rate (₹)	Amount (₹)
Material-A	900 kg.	43.00	38,700
Material-B	650 kg.	32.50	21,125
Skilled labour	1,200 hours	35.50	42,600
Unskilled labour	860 hours	23.00	19,780

You are required to calculate:

- Material Cost Variance;
- Material Price Variance;
- Material Mix Variance;
- Material Yield Variance;
- Labour Cost Variance;
- Labour Efficiency Variance and
- Labour Yield Variance.

### Marginal Costing

9. The following figures are available from the records of XYZ Company as at 31<sup>st</sup> March.

	2017 (₹ in lakhs)	2018 (₹ in lakhs)
Sales	200	250
Profit	30	45

Calculate:

- The P/V ratio and total fixed expenses.
- The break-even level of sales.
- Sales required to earn a profit of ₹ 70 lakhs.

### Budget and Budgetary Control

10. Usha Ltd. manufactures two products called 'M' and 'N'. Both products use a common raw material Z. The raw material Z is purchased @ ₹ 36 per kg from the market. The company has decided to review inventory management policies for the forthcoming year.

The following information has been extracted from departmental estimates for the year ended 31<sup>st</sup> March 2018 (the budget period):

	Product M	Product N
Sales (units)	28,000	13,000

Finished goods stock increase by year-end	320	160
Post-production rejection rate (%)	4	6
Material Z usage (per completed unit, net of wastage)	5 kg	6 kg
Material Z wastage (%)	10	5

Additional information:

- Usage of raw material Z is expected to be at a constant rate over the period.
- Annual cost of holding one unit of raw material in stock is 11% of the material cost.
- The cost of placing an orders is ₹ 320 per order.
- The management of Usha Ltd. has decided that there should not be more than 40 orders in a year for the raw material Z.

**Required:**

- (a) Prepare functional budgets for the year ended 31st March 2018 under the following headings:
- (i) Production budget for Products M and N (in units).
  - (ii) Purchases budget for Material Z (in kgs and value).
- (b) Calculate the Economic Order Quantity for Material Z (in kgs).
- (c) If there is a sole supplier for the raw material Z in the market and the supplier do not sale more than 4,000 kg. of material Z at a time. Keeping the management purchase policy and production quantity mix into consideration, calculate the maximum number of units of Product M and N that could be produced.

### SUGGESTED HINTS/ANSWERS

1. (i) Calculation of Economic Order Quantity:

$$EOQ = \sqrt{\frac{2 \times A \times O}{C_i}} = \sqrt{\frac{2 \times (60,000 \text{ packs} \times 12 \text{ months}) \times ₹ 240}{₹ 228 \times 10\%}}$$

$$= 3,893.3 \text{ packs or } 3,893 \text{ packs.}$$

- (ii) Number of orders per year

$$\frac{\text{Annual requirements}}{\text{E.O.Q}} = \frac{7,20,000 \text{ packs}}{3,893 \text{ packs}} = 184.9 \text{ or } 185 \text{ orders a year}$$



## (iii) Ordering and storage costs

	(₹)
Ordering costs :- 185 orders × ₹ 240	44,400.00
Storage cost :- ½ (3,893 packs × 10% of ₹228)	<u>44,380.20</u>
Total cost of ordering & storage	<u>88,780.20</u>

## (iv) Timing of next order

(a) Day's requirement served by each order.

$$\text{Number of days requirements} = \frac{\text{No. of working days}}{\text{No. of order in a year}} = \frac{360 \text{ days}}{185 \text{ orders}} = 1.94 \text{ days}$$

supply.

This implies that each order of 3,893 packs supplies for requirements of 1.94 days only.

(b) Days requirement covered by inventory

$$= \frac{\text{Units in inventory}}{\text{Economic order quantity}} \times (\text{Day's requirement served by an order})$$

$$\therefore \frac{10,033 \text{ packs}}{3,893 \text{ packs}} \times 1.94 \text{ days} = 5 \text{ days requirement}$$

(c) Time interval for placing next order

Inventory left for day's requirement – Average lead time of delivery

$$5 \text{ days} - 5 \text{ days} = 0 \text{ days}$$

This means that next order for the replenishment of supplies has to be placed immediately.

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

$$\therefore \text{ Output by new recruits} = 60\% \text{ of } 5,000 = 3,000 \text{ units}$$

$$\text{Loss of output} = 5,000 - 3,000 = 2,000 \text{ units}$$

$$\begin{aligned} \text{Total loss of output} &= \text{Due to delay recruitment} + \text{Due to inexperience} \\ &= 10,000 + 2,000 = 12,000 \text{ units} \end{aligned}$$

$$\text{Contribution per unit} = 20\% \text{ of } ₹180 = ₹ 36$$

$$\text{Total contribution lost} = ₹36 \times 12,000 \text{ units} = ₹ 4,32,000$$

$$\text{Cost of repairing defective units} = 3,000 \text{ units} \times 0.2 \times ₹ 25 = ₹ 15,000$$

**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 2017-18	9,00,000

3. (i) Amount of under/ over absorption of production overheads during the period of first six months of the year 2017-2018:

	Amount (₹)	Amount (₹)
Total production overheads actually incurred during the period		24,88,200
Less: Amount paid to worker as per court order	1,28,000	
Expenses of previous year booked in the current year	1,200	
Wages paid for the strike period under an award	44,000	
Obsolete stores written off	6,700	(1,79,900)
		23,08,300
Less: Production overheads absorbed as per machine hour rate (1,16,000 hours × ₹20*)		23,20,000
Amount of over absorbed production overheads		11,700

$$\text{*Budgeted Machine hour rate (Blanket rate)} = \frac{\text{₹44,00,000}}{2,20,000 \text{ hours}} = \text{₹ 20 per hour}$$

- (ii) **Accounting treatment of over absorbed production overheads:** As, one fourth of the over absorbed overheads were due to defective production policies, this being abnormal, hence should be transferred to Costing Profit and Loss Account.

$$\text{Amount to be transferred to Costing Profit and Loss Account} = (11,700 \times \frac{1}{4}) \text{ ₹ } 2,925$$

Balance of over absorbed production overheads should be distributed over Works in progress, finished goods and Cost of sales by applying supplementary rate\*.

$$\text{Amount to be distributed} = (11,700 \times \frac{3}{4}) \text{ ₹ } 8,775$$

$$\text{Supplementary rate} = \frac{\text{₹ } 8,775}{33,000 \text{ units}} = \text{₹ } 0.2659 \text{ per unit}$$

- (iii) Apportionment of under absorbed production overheads over WIP, Finished goods and Cost of sales:

	Equivalent completed units	Amount (₹)
Work-in-Progress (18,000 units × 50% × ₹ 0.2659)	9,000	2,393
Finished goods (2,400 units × ₹ 0.2659)	2,400	638

Cost of sales (21,600 units × ₹ 0.2659)	21,600	5,744
Total	33,000	8,775

4. **Cost Ledger Control Account**

Particulars	(₹)	Particulars	(₹)
To Store Ledger Control A/c	11,000	By Opening Balance	7,00,000
To Balance c/d	9,84,600	By Store ledger control A/c	1,36,000
		By Manufacturing Overhead Control A/c	91,000
		By Wages Control A/c	68,600
	9,95,600		9,95,600

**Stores Ledger Control Account**

Particulars	(₹)	Particulars	(₹)
To Opening Balance	3,20,000	By WIP Control A/c	1,26,000
To Cost ledger control A/c	1,36,000	By Cost ledger control A/c (Returns)	11,000
		By Balance c/d	3,19,000
	4,56,000		4,56,000

**WIP Control Account**

Particulars	(₹)	Particulars	(₹)
To Opening Balance	1,52,000	By Finished Stock Ledger Control A/c	2,35,500
To Wages Control A/c	48,000	By Balance c/d	1,76,500
To Stores Ledger Control A/c	1,26,000		
To Manufacturing Overhead Control A/c	86,000		
	4,12,000		4,12,000

**Finished Stock Ledger Control Account**

Particulars	(₹)	Particulars	(₹)
To Opening Balance	2,56,000	By Cost of Sales	1,68,000
To WIP Control A/c	2,35,500	By Balance c/d	3,31,500
To Cost of Sales A/c (Sales Return)	8,000		
	4,99,500		4,99,500

**Manufacturing Overhead Control Account**

Particulars	(₹)	Particulars	(₹)
To Cost Ledger Control A/c	91,000	By Opening Balance	28,000
To Wages Control A/c	20,600	By WIP Control A/c	86,000
To Over recovery c/d	2,400		
	1,14,000		1,14,000

**Wages Control Account**

Particulars	(₹)	Particulars	(₹)
To Transfer to Cost Ledger Control A/c	68,600	By WIP Control A/c	48,000
		By Manufacturing Overhead Control A/c	20,600
	68,600		68,600

**Cost of Sales Account**

Particulars	(₹)	Particulars	(₹)
To Finished Stock Ledger Control A/c	1,68,000	By Finished Stock Ledger Control A/c (Sales return)	8,000
		By Balance c/d	1,60,000
	1,68,000		1,68,000

**Trial Balance**

	(₹)	(₹)
Stores Ledger Control A/c	3,19,000	
WIP Control A/c	1,76,500	
Finished Stock Ledger Control A/c	3,31,500	
Manufacturing Overhead Control A/c	--	2,400
Cost of Sales A/c	1,60,000	
Cost ledger control A/c	--	9,84,600
	9,87,000	9,87,000

## 5. Statement of cost per batch and per order

No. of batch = 600 units ÷ 50 units = 12 batches

	Particulars	Cost per batch (₹)	Total Cost (₹)
	Direct Material Cost	5,000.00	60,000
	Direct Wages	500.00	6,000
	Oven set-up cost	750.00	9,000
	Add: Production Overheads (20% of Direct wages)	100.00	1,200
	<b>Total Production cost</b>	<b>6,350.00</b>	<b>76,200</b>
	Add: S&D and Administration overheads (10% of Total production cost)	635.00	7,620
	<b>Total Cost</b>	<b>6,985.00</b>	<b>83,820</b>
	Add: Profit (1/3 <sup>rd</sup> of total cost)	2,328.33	27,940
<b>(i)</b>	<b>Sales price</b>	<b>9,313.33</b>	<b>1,11,760</b>
	No. of units in batch	50 units	
<b>(ii)</b>	<b>Cost per unit</b> (₹6,985 ÷ 50 units)	<b>139.70</b>	
	<b>Selling price per unit</b> (9,313.33 ÷ 50 units)	<b>186.27</b>	

**(iii)** If the order is for 605 cakes, then selling price per cake would be as below:

Particulars	Total Cost (₹)
Direct Material Cost	60,500
Direct Wages (₹500 × 13 batches)	6,500
Oven set-up cost (₹750 × 13 batches)	9,750
Add: Production Overheads (20% of Direct wages)	1,300
<b>Total Production cost</b>	<b>78,050</b>
Add: S&D and Administration overheads (10% of Total production cost)	7,805
<b>Total Cost</b>	<b>85,855</b>
Add: Profit (1/3 <sup>rd</sup> of total cost)	28,618
<b>Sales price</b>	<b>1,14,473</b>
No. of units	605 units
<b>Selling price per unit</b> (₹ 1,14,473 ÷ 605 units)	<b>189.21</b>

## 6. (a) Calculation of Raw Material inputs during the month:

Quantities Entering Process	Litres	Quantities Leaving Process	Litres
Opening WIP	800	Transfer to Finished Goods	4,200
Raw material input (balancing figure)	5,360	Process Losses	1,800
		Closing WIP	160
	6,160		6,160

## (b) Calculation of Normal Loss and Abnormal Loss/Gain

	Litres
Total process losses for month	1,800
Normal Loss (10% input)	536
Abnormal Loss (balancing figure)	1,264

## (c) Calculation of values of Raw Material, Labour and Overheads added to the process:

	Material	Labour	Overheads
Cost per equivalent unit	₹23.00	₹7.00	₹9.00
Equivalent units (litre) (refer the working note)	4,824	4,952	5,016
Cost of equivalent units	₹1,10,952	₹34,664	₹45,144
Add: Scrap value of normal loss (536 units × ₹ 15)	₹8,040	--	--
Total value added	₹1,18,992	₹34,664	₹45,144

## Workings:

## Statement of Equivalent Units (litre):

Input Details	Units	Output details	Units	Equivalent Production					
				Material		Labour		Overheads	
				Units	(%)	Units	(%)	Units	(%)
Opening WIP	800	Units completed:							
Units introduced	5,360	- Opening WIP	800	--	--	240	30	320	40

		- Fresh inputs	3,400	3,400	100	3,400	100	3,400	100
		Normal loss	536	--	--	--	--	--	--
		Abnormal loss	1,264	1,264	100	1,264	100	1,264	100
		Closing WIP	160	160	100	48	30	32	20
	6,160		6,160	4,824		4,952		5,016	

(d) **Process Account for Month**

	Litres	Amount (₹)		Litres	Amount (₹)
To Opening WIP	800	26,640	By Finished goods	4,200	1,63,800
To Raw Materials	5,360	1,18,992	By Normal loss	536	8,040
To Wages	--	34,664	By Abnormal loss	1,264	49,296
To Overheads	--	45,144	By Closing WIP	160	4,304
	6,160	2,25,440		6,160	2,25,440

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	15	2



	$\left( \frac{₹ 1,80,000}{18,000 \text{ kg}} \right)$	$\left( \frac{₹ 1,50,000}{10,000 \text{ kg}} \right)$	$\left( \frac{₹ 1,08,000}{54,000 \text{ kg}} \right)$
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	50	18
	$\left( \frac{₹ 12,24,000}{17,000 \text{ kg}} \right)$	$\left( \frac{₹ 2,50,000}{5,000 \text{ kg}} \right)$	$\left( \frac{₹ 7,92,000}{44,000 \text{ kg}} \right)$

## 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	2,15,000	90,000	3,50,000
	(₹ 45 x 1,000 kg)	(₹ 43 x 5,000 kg)	(₹9x10,000 kg)	

## (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. Material Variances:

Material	SQ (WN-1)	SP (₹)	SQ × SP (₹)	RSQ (WN-2)	RSQ × SP (₹)	AQ	AQ × SP (₹)	AP (₹)	AQ × AP (₹)
A	940 kg.	45.00	42,300	886 kg.	39,870	900 kg.	40,500	43.00	38,700
B	705 kg.	30.00	21,150	664 kg.	19,920	650 kg.	19,500	32.50	21,125
	1645 kg		63,450	1550 kg	59,790	1550 kg	60,000		59,825

## WN-1: Standard Quantity (SQ):

$$\text{Material A-} \left( \frac{800 \text{ kg.}}{0.9 \times 1,400 \text{ kg.}} \times 1,480 \text{ kg.} \right) = 939.68 \text{ or } 940 \text{ kg.}$$

$$\text{Material B-} \left( \frac{600 \text{ kg.}}{0.9 \times 1,400 \text{ kg.}} \times 1,480 \text{ kg.} \right) = 704.76 \text{ or } 705 \text{ kg.}$$

## WN- 2: Revised Standard Quantity (RSQ):

$$\text{Material A-} \left( \frac{800 \text{ kg.}}{1,400 \text{ kg.}} \times 1,550 \text{ kg.} \right) = 885.71 \text{ or } 886 \text{ kg.}$$

$$\text{Material B-} \left( \frac{600 \text{ kg.}}{1,400 \text{ kg.}} \times 1,550 \text{ kg.} \right) = 664.28 \text{ or } 664 \text{ kg.}$$

$$\begin{aligned} \text{(a) Material Cost Variance (A + B)} &= \{(SQ \times SP) - (AQ \times AP)\} \\ &= \{63,450 - 59,825\} = 3,625 \text{ (F)} \end{aligned}$$

$$\begin{aligned} \text{(b) Material Price Variance (A + B)} &= \{(AQ \times SP) - (AQ \times AP)\} \\ &= \{60,000 - 59,825\} = 175 \text{ (F)} \end{aligned}$$

- (c) Material Mix Variance (A + B) = {(RSQ × SP) – (AQ × SP)}  
= {59,790 – 60,000} = 210 (A)
- (d) Material Yield Variance (A + B) = {(SQ × SP) – (RSQ × SP)}  
= {63,450 – 59,790} = 3,660 (F)

**Labour Variances:**

Labour	SH (WN-3)	SR (₹)	SH × SR (₹)	RSH (WN-4)	RSH × SR (₹)	AH	AH × SR (₹)	AR (₹)	AH × AR (₹)
Skilled	1,116 hrs	37.50	41,850	1144	42,900	1,200	45,000	35.50	42,600
Unskilled	893 hrs	22.00	19,646	916	20,152	860	18,920	23.00	19,780
	2,009 hrs		61,496	2,060	63,052	2,060	63,920		62,380

**WN- 3: Standard Hours (SH):**

$$\text{Skilled labour- } \left( \frac{0.95 \times 1,000 \text{ hr.}}{0.90 \times 1,400 \text{ kg.}} \times 1,480 \text{ kg.} \right) = 1,115.87 \text{ or } 1,116 \text{ hrs.}$$

$$\text{Unskilled labour- } \left( \frac{0.95 \times 800 \text{ hr.}}{0.90 \times 1,400 \text{ kg.}} \times 1,480 \text{ kg.} \right) = 892.69 \text{ or } 893 \text{ hrs.}$$

**WN- 4: Revised Standard Hours (RSH):**

$$\text{Skilled labour- } \left( \frac{1,000 \text{ hr.}}{1,800 \text{ hr.}} \times 2,060 \text{ hr.} \right) = 1,144.44 \text{ or } 1,144 \text{ hrs.}$$

$$\text{Unskilled labour- } \left( \frac{800 \text{ hr.}}{1,800 \text{ hr.}} \times 2,060 \text{ hr.} \right) = 915.56 \text{ or } 916 \text{ hrs.}$$

- (e) Labour Cost Variance (Skilled + Unskilled) = {(SH × SR) – (AH × AR)}  
= {61,496 – 62,380} = 884 (A)
- (f) Labour Efficiency Variance (Skilled + Unskilled) = {(SH × SR) – (AH × SR)}  
= {61,496 – 63,920} = 2,424 (A)
- (g) Labour Yield Variance (Skilled + Unskilled) = {(SH × SR) – (RSH × SR)}  
= {61,496 – 63,052} = 1,556 (A)

**9. (i) Profit-Volume (P/V) Ratio:**

$$= \frac{\text{Change in Profit}}{\text{Change in Sales}} \times 100 = \frac{\text{Profit in 2018} - \text{Profit in 2017}}{\text{Sales in 2018} - \text{Sales in 2017}} \times 100$$

$$= \frac{\text{₹ 45 lakhs} - \text{₹ 30 lakhs}}{\text{₹ 250 lakhs} - \text{₹ 200 lakhs}} \times 100 = 30\%$$

**Fixed Expenses:**

	2017 (₹ in lakhs)	OR	2018 (₹ in lakhs)
Contribution	60 (30% of 200)		75 (30% of 250)
Less: Profit	30		45
Fixed Expenses	30		30

**(ii) Break-even level of sales:**

$$= \frac{\text{Fixed Expenses}}{\text{P/V ratio}} = \frac{\text{₹ 30 lakh}}{30\%} = \text{₹ 100 lakhs}$$

**(iii) Sales required to earn a profit of ₹ 70 lakhs:**

$$= \frac{\text{Fixed Expenses} + \text{Desired profit}}{\text{P/V ratio}}$$

$$= \frac{\text{₹ 30 lakhs} + \text{₹ 70 lakhs}}{30\%} = \text{₹ 333.33 lakhs}$$

**10. (a) (i) Production Budget (in units) for the year ended 31<sup>st</sup> March 2018**

	Product M	Product N
Budgeted sales (units)	28,000	13,000
Add: Increase in closing stock	320	160
No. good units to be produced	28,320	13,160
Post production rejection rate	4%	6%
No. of units to be produced	29,500 $\left( \frac{28,320}{0.96} \right)$	14,000 $\left( \frac{13,160}{0.94} \right)$

**(ii) Purchase budget (in kgs and value) for Material Z**

	Product M	Product N
No. of units to be produced	29,500	14,000
Usage of Material Z per unit of production	5 kg.	6 kg.
Material needed for production	1,47,500 kg.	84,000 kg.

Materials to be purchased	1,63,889 kg. $\left( \frac{1,47,500}{0.90} \right)$	88,421 kg. $\left( \frac{84,000}{0.95} \right)$
Total quantity to be purchased	2,52,310 kg.	
Rate per kg. of Material Z	₹ 36	
Total purchase price	₹ 90,83,160	

**(b) Calculation of Economic Order Quantity for Material Z**

$$EOQ = \sqrt{\frac{2 \times 2,52,310 \text{ kg.} \times ₹320}{₹36 \times 11\%}} = \sqrt{\frac{16,14,78,400}{₹3.96}} = 6,385.72 \text{ kg.}$$

- (c) Since, the maximum number of order per year cannot be more than 40 orders and the maximum quantity per order that can be purchased is 4,000 kg. Hence, the total quantity of Material Z that can be available for production:

$$= 4,000 \text{ kg.} \times 40 \text{ orders} = 1,60,000 \text{ kg.}$$

	Product M	Product N
Material needed for production to maintain the same production mix	1,03,929 kg. $\left( 1,60,000 \times \frac{1,63,889}{2,52,310} \right)$	56,071 kg. $\left( 1,60,000 \times \frac{88,421}{2,52,310} \right)$
Less: Process wastage	10,393 kg.	2,804 kg.
Net Material available for production	93,536 kg.	53,267 kg.
Units to be produced	18,707 units $\left( \frac{93,536 \text{ kg.}}{5 \text{ kg.}} \right)$	8,878 units $\left( \frac{53,267 \text{ kg.}}{6 \text{ kg.}} \right)$

**PAPER 3: COST ACCOUNTING AND FINANCIAL MANAGEMENT****PART II: FINANCIAL MANAGEMENT****QUESTIONS****Time Value of Money**

1. You need a sum of ₹ 1,00,000 at the end of 10 years. You know that the best you can do is to deposit some lump sum amount today at 6% rate of interest or to make equal payments into a bank account, starting a year from now on which you can earn 6% interest. Find out

- (i) What amount to be deposited today or  
(ii) What amount must be deposited annually?

(Compound value factor and compound value factor of annuity of Re. 1 for 10 year @ 6% is 1.791 and 13.181 respectively)

**Ratio Analysis**

2. Based on the following particulars List out various assets and liabilities and prepare a Balance sheet of Tirupati Ltd.

Fixed assets turnover ratio	8 times
Capital turnover ratio	2 times
Inventory Turnover	8 times
Receivable turnover	4 times
Payable turnover	6 times
GP Ratio	25%

Gross profit during the year amounts to ₹ 8,00,000. There is no long-term loan or overdraft. Reserve and surplus amount to ₹ 2,00,000. Ending inventory of the year is ₹ 20,000 above the beginning inventory.

**Fund Flow Analysis**

3. Balance Sheets of RST Limited as on March 31, 20X8 and March 31, 20X9 are as under:

Liabilities	31.3.20X8 (₹)	31.3.20X9 (₹)	Assets	31.3.20X8 (₹)	31.3.20X9 (₹)
Equity Share Capital (₹10 face value per share)	10,00,000	12,00,000	Land & Building	6,00,000	7,00,000
General Reserve	3,50,000	2,00,000	Plant & Machinery	9,00,000	11,00,000

9% Preference Share Capital	3,00,000	5,00,000	Investments (Long-term)	2,50,000	2,50,000
Share Premium A/c	25,000	4,000	Stock	3,60,000	3,50,000
Profit & Loss A/c	2,00,000	3,00,000	Debtors	3,00,000	3,90,000
8% Debentures	3,00,000	1,00,000	Cash & Bank	1,00,000	95,000
Creditors	2,05,000	3,00,000	Prepaid Expenses	15,000	20,000
Bills Payable	45,000	81,000	Advance Tax Payment	80,000	1,05,000
Provision for Tax	70,000	1,00,000	Preliminary Expenses	40,000	35,000
Proposed Dividend	1,50,000	2,60,000			
	26,45,000	30,45,000		26,45,000	30,45,000

Additional information:

- (i) Depreciation charged on building and plant and machinery during the year 20X8-X9 were ₹ 50,000 and ₹ 1,20,000 respectively.
- (ii) During the year an old machine costing ₹ 1,50,000 was sold for ₹ 32,000. Its written down value was ₹ 40,000 on date of sale.
- (iii) During the year, income tax for the year 20X7-X8 was assessed at ₹76,000. A cheque of ₹ 4,000 was received along with the assessment order towards refund of income tax paid in excess, by way of advance tax in earlier years.
- (iv) Proposed dividend for 20X7-X8 was paid during the year 20X8-X9.
- (v) 9% Preference shares of ₹ 3,00,000, which were due for redemption, were redeemed during the year 20X8-X9 at a premium of 5%, out of the proceeds of fresh issue of 9% Preference shares.
- (vi) Bonus shares were issued to the existing equity shareholders at the rate of one share for every five shares held on 31.3.20X8 out of general reserves.
- (vii) Debentures were redeemed at the beginning of the year at a premium of 3%.
- (viii) Interim dividend paid during the year 20X8-X9 was ₹ 50,000.

Required:

- (a) Schedule of Changes in Working Capital; and
- (b) Fund Flow Statement for the year ended March 31, 20X9.

**Cost of Capital**

4. Navya Limited wishes to raise additional capital of ₹10 lakhs for meeting its modernisation plans. It has ₹ 3,00,000 in the form of retained earnings available for investments purposes. The following are the further details:

Debt/equity mix	40%/60%
Cost of debt (before tax)	
Upto ₹ 1,80,000	10%
Beyond ₹ 1,80,000	16%
Earnings per share	₹ 4
Dividend pay out	₹ 2
Expected growth rate in dividend	10%
Current market price per share	₹ 44
Tax rate	50%

You are required:

- To ascertain the pattern for raising the additional finance.
- To calculate the post-tax average cost of additional debt.
- To calculate the cost of retained earnings and cost of equity, and
- Find out the overall weighted average cost of capital (after tax).

**Capital Structure Decisions**

5. Company P and Q are identical in all respects including risk factors except for debt/equity, company P having issued 10% debentures of ₹ 18 lakhs while company Q is unlevered. Both the companies earn 20% before interest and taxes on their total assets of ₹ 30 lakhs.

Assuming a tax rate of 50% and capitalization rate of 15% from an all-equity company. Calculate the value of companies P and Q using (i) Net Income Approach and (ii) Net Operating Income Approach.

**Leverage**

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

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



Fixed Cost:

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

Capital Structure:

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

### Capital Budgeting

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

Year	Project A	Project B	Discounting factor @ 16%
1	--	60,000	0.862
2	30,000	84,000	0.743
3	1,32,000	96,000	0.641
4	84,000	1,02,000	0.552
5	84,000	90,000	0.476

You are required to calculate for each project:

- (i) Discounted payback period
- (ii) Profitability index
- (iii) Net present value

### Management of Payables (Creditors)

8. A Ltd. is in the manufacturing business and it acquires raw material from X Ltd. on a regular basis. As per the terms of agreement the payment must be made within 40 days of purchase. However, A Ltd. has a choice of paying ₹ 98.50 per ₹ 100 it owes to X Ltd. on or before 10<sup>th</sup> day of purchase. Examine Whether A Ltd. should accept the offer of discount assuming average billing of A Ltd. with X Ltd. is ₹ 10,00,000 and an alternative investment yield a return of 15% and company pays the invoice.

**Financing of Working Capital**

9. Following information is forecasted by the Puja Limited for the year ending 31<sup>st</sup> March, 20X8:

	Balance as at 1 <sup>st</sup> April, 20×7 (₹)	Balance as at 31 <sup>st</sup> March, 20×8 (₹)
Raw Material	45,000	65,356
Work-in-progress	35,000	51,300
Finished goods	60,181	70,175
Debtors	1,12,123	1,35,000
Creditors	50,079	70,469
Annual purchases of raw material (all credit)		4,00,000
Annual cost of production		7,50,000
Annual cost of goods sold		9,15,000
Annual operating cost		9,50,000
Annual sales (all credit)		11,00,000

You may take one year as equal to 365 days.

You are required to calculate:

- (i) Net operating cycle period.
- (ii) Number of operating cycles in the year.
- (iii) Amount of working capital requirement using operating cycles.

**10. Miscellaneous**

- (a) "The profit maximization is not an operationally feasible criterion". Discuss
- (b) Explain the followings:
  - (i) Bridge Finance
  - (ii) Floating Rate Bonds
  - (iii) Packing Credit.
- (c) "Financial Leverage is a double edged sword" Discuss

## SUGGESTED ANSWERS/HINTS

$$1. \quad (i) \quad PV = \frac{FV}{(1+k)^n} \quad \text{or, } PV = \frac{₹1,00,000}{(1+0.06)^{10}}$$

$$= ₹ 55,839.48$$

$$(ii) \quad FVA(k,n) = A \left[ \frac{(1+k)^n - 1}{k} \right]$$

$$A = \frac{FVA(k,n)}{\left[ \frac{(1+k)^n - 1}{k} \right]} = \frac{₹1,00,000}{13.181} = ₹ 7,586.68$$

$$2. \quad (a) \quad \text{G.P. ratio} = \frac{\text{Gross Profit}}{\text{Sales}} = 25\%$$

$$\text{Sales} = \frac{\text{Gross Profit}}{25} \times 100 = \frac{₹ 8,00,000}{25} \times 100 = ₹ 32,00,000$$

$$(b) \quad \text{Cost of Sales} = \text{Sales} - \text{Gross profit}$$

$$= ₹ 32,00,000 - ₹ 8,00,000$$

$$= ₹ 24,00,000$$

$$(c) \quad \text{Receivable turnover} = \frac{\text{Sales}}{\text{Receivables}} = 4$$

$$= \text{Receivables} = \frac{\text{Sales}}{4} = \frac{₹ 32,00,000}{4} = ₹ 8,00,000$$

$$(d) \quad \text{Fixed assets turnover} = \frac{\text{Cost of Sales}}{\text{Fixed Assets}} = 8$$

$$\text{Fixed assets} = \frac{\text{Cost of Sales}}{8} = \frac{₹ 24,00,000}{8} = ₹ 3,00,000$$

$$(e) \quad \text{Inventory turnover} = \frac{\text{Cost of Sales}}{\text{Average Stock}} = 8$$

$$\text{Average Stock} = \frac{\text{Cost of Sales}}{8} = \frac{₹ 24,00,000}{8} = ₹ 3,00,000$$

$$\begin{aligned} \text{Average Stock} &= \frac{\text{Opening Stock} + \text{Closing Stock}}{2} \\ \text{Average Stock} &= \frac{\text{Opening Stock} + \text{Opening Stock} + 20,000}{2} \\ \text{Average Stock} &= \text{Opening Stock} + ₹ 10,000 \\ \text{Opening Stock} &= \text{Average Stock} - ₹ 10,000 \\ &= ₹ 3,00,000 - ₹ 10,000 \\ &= ₹ 2,90,000 \\ \text{Closing Stock} &= \text{Opening Stock} + ₹ 20,000 \\ &= ₹ 2,90,000 + ₹ 20,000 \\ &= ₹ 3,10,000 \\ \text{(f) Payable turnover} &= \frac{\text{Purchase}}{\text{Creditors}} = 6 \\ \text{Purchases} &= \text{Cost of Sales} + \text{Increase in Stock} \\ &= ₹ 24,00,000 + ₹ 20,000 \\ &= ₹ 24,20,000 \\ \text{Payables} &= \frac{\text{Purchase}}{6} = \frac{₹ 24,20,000}{6} = ₹ 4,03,333 \\ \text{(g) Capital turnover} &= \frac{\text{Cost of Sales}}{\text{Capital Employed}} = 2 \\ \text{Capital Employed} &= \frac{\text{Cost of Sales}}{2} = \frac{₹ 24,00,000}{2} = ₹ 12,00,000 \\ \text{(h) Share Capital} &= \text{Capital Employed} - \text{Reserves \& Surplus} \\ &= ₹ 12,00,000 - ₹ 2,00,000 = ₹ 10,00,000 \end{aligned}$$

**Balance Sheet of Tirupati Ltd as on**

Liabilities	Amount (₹)	Assets	Amount (₹)
Share Capital	10,00,000	Fixed Assets	3,00,000
Reserve & Surplus	2,00,000	Closing Inventories	3,10,000
Payables	4,03,333	Receivables	8,00,000

		Other Current Assets	1,93,333
	16,03,333		16,03,333

(Fixed Asset turnover, inventory turnover capital turnover is calculated on cost of sales)

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

Particulars	31st March		Working Capital	
	20X8 (₹)	20X9 (₹)	Increase (₹)	Decrease (₹)
<b>A. Current Assets:</b>				
Stock	3,60,000	3,50,000	--	10,000
Sundry Debtors	3,00,000	3,90,000	90,000	--
Prepaid expenses	15,000	20,000	5,000	--
Cash and Bank	1,00,000	95,000	--	5,000
<b>Total (A)</b>	<b>7,75,000</b>	<b>8,55,000</b>		
<b>B. Current Liabilities:</b>				
Sundry Creditors	2,05,000	3,00,000	--	95,000
Bills Payables	45,000	81,000	--	36,000
<b>Total (B)</b>	<b>2,50,000</b>	<b>3,81,000</b>		
Working Capital (A – B)	5,25,000	4,74,000		
Decrease in Working Capital		51,000	51,000	
<b>Total</b>	<b>5,25,000</b>	<b>5,25,000</b>	<b>1,46,000</b>	<b>1,46,000</b>

(b) **Funds Flow Statement for the year ending 31<sup>st</sup> March, 20X9**

	(₹)
<b>A. Sources of Funds:</b>	
(i) Fund from Business Operations	7,49,000
(ii) Proceeds from issue of 9% Preference shares	5,00,000
(iii) Proceeds from sale of Plant & Machinery	32,000
(iv) Income tax refund	4,000
Total sources	12,85,000
<b>B. Application of Funds:</b>	
(i) Purchase of Land and Building	1,50,000

(ii) Purchase of Plant and Machinery	3,60,000
(iii) Redemption of 8% Debentures	2,06,000
(iv) Redemption of 9% Preference shares	3,15,000
(v) Payment of income tax assessed	1,05,000
(vi) Payment of Interim dividend	50,000
(vii) Payment of dividend	1,50,000
Total uses	13,36,000
Net Decrease in Working Capital (A – B)	51,000

**Working Notes:****(1) Computation of Funds from Business Operation**

	(₹)
Profit & Loss as on March 31, 20X9	3,00,000
<i>Add:</i> Depreciation on Land and Building	50,000
Depreciation on Plant and Machinery	1,20,000
Loss on sale of Plant and Machinery	8,000
Preliminary expenses written off	5,000
Transfer to General Reserve	50,000
Proposed dividend	2,60,000
Provision for tax	1,06,000
Interim dividend paid	50,000
	9,49,000
<i>Less:</i> Profit and loss as on March 31, 20X8	2,00,000
Fund from Operations	7,49,000

**(2) Plant & Machinery A/c**

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

## (3) Land and Building A/c

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

## (4) Advance Tax Payment A/c

	(₹)		(₹)
To Balance b/d	80,000	By Provision for taxation A/c	76,000
To Bank (paid for 08-09)	1,05,000	By Bank (Refund of tax)	4,000
		By Balance c/d	1,05,000
	1,85,000		1,85,000

## (5) Provision for Taxation A/c

	(₹)		(₹)
To Advance tax payment A/c	76,000	By Balance b/d	70,000
To Balance c/d	1,00,000	By P/L A/c (additional provision for 20X7-X8)	6,000
		By P/L A/c (Provision for X8-X9)	1,00,000
	1,76,000		1,76,000

## (6) 8% Debentures A/c

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

## (7) 9% Preference Share Capital A/c

	(₹)		(₹)
To Bank A/c (redemption) (3,00,000 x 105%)	3,15,000	By Balance b/d	3,00,000
To Balance c/d	5,00,000	By Premium on redemption	15,000

		of Preference shares A/c	
		By Bank (Issue)	5,00,000
	8,15,000		8,15,000

**(8) Securities Premium A/c**

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

**(9) General Reserve A/c**

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

Provision for tax and Advance tax may be taken as current liability and current assets respectively.

**4. (a) Pattern of Raising Additional Finance**

$$\text{Equity} = 10,00,000 \times 60/100 = ₹ 6,00,000$$

$$\text{Debt} = 10,00,000 \times 40/100 = ₹ 4,00,000$$

Capital structure after Raising Additional Finance

Sources of fund	Amount (₹)
Shareholder's funds	
Equity capital (6,00,000 – 3,00,000)	3,00,000
Retained earnings	3,00,000
Debt at 10% p.a.	1,80,000
Debt at 16% p.a. (4,00,000 – 1,80,000)	2,20,000
Total funds	10,00,000



**(b) Post-tax Average Cost of Additional Debt**

$K_d = i(1 - t)$ , where ' $K_d$ ' is cost of debt, ' $i$ ' is interest and ' $t$ ' is tax rate.

On ₹ 1,80,000 = 10% (1 - 0.5) = 5% or 0.05

On ₹ 2,20,000 = 16% (1 - 0.5) = 8% or 0.08

Average Cost of Debt (Post tax) i.e.

$$K_d = \frac{1,80,000 \times 0.05 + 2,20,000 \times 0.08}{4,00,000} \times 100 = 6.65\% \text{ (approx)}$$

**(c) Cost of Retained Earnings and Cost of Equity applying Dividend Growth Model**

$$K_e = \frac{D_1}{P_0} + g \quad \text{or} \quad \frac{D_0 (1+g)}{P_0} + g$$

$$\text{Then, } K_e = \frac{2.1}{44} + 0.10 = \frac{2.2}{44} + 0.10 = 0.15 \text{ or } 15\%$$

**(d) Overall Weighted Average Cost of Capital (WACC) (After Tax)**

Particulars	Amount (₹)	Weights	Cost of Capital	WACC
Equity (including retained earnings)	6,00,000	0.60	15%	9.00
Debt	4,00,000	0.40	6.65%	2.66
Total	10,00,000	1.00		11.66

**5. (i) Valuation under Net Income Approach**

Particulars	P	Q
	Amount (₹)	Amount (₹)
Earnings before Interest & Tax (EBIT) (20% of ₹ 30,00,000)	6,00,000	6,00,000
Less: Interest (10% of ₹ 18,00,000)	1,80,000	
Earnings before Tax (EBT)	4,20,000	6,00,000
Less: Tax @ 50%	2,10,000	3,00,000
Earnings after Tax (EAT) (available to equity holders)	2,10,000	3,00,000
Value of equity (capitalized @ 15%)	14,00,000 (2,10,000 × 100/15)	20,00,000 (3,00,000 × 100/15)

Add: Total Value of debt	18,00,000	Nil
Total Value of Company	32,00,000	20,00,000

## (ii) Valuation of Companies under Net Operating Income Approach

Particulars	P Amount (₹)	Q Amount (₹)
Capitalisation of earnings at 15% $\left( \frac{₹6,00,000(1-0.5)}{0.15} \right)$	20,00,000	20,00,000
Less: Value of debt {18,00,000 (1 - 0.5)}	9,00,000	Nil
Value of equity	11,00,000	20,00,000
Add: Total Value of debt	18,00,000	Nil
Total Value of Company	29,00,000	20,00,000

## 6. (i) Operating leverages:

Particulars	Situation-I (₹)	Situation-II (₹)
Sales (S) (3,000 units @ ₹ 30/- per unit)	90,000	90,000
Less: Variable Cost (VC) @ ₹15 per unit	<u>(45,000)</u>	<u>(45,000)</u>
Contribution (C)	45,000	45,000
Less: Fixed Cost (FC)	<u>15,000</u>	<u>20,000</u>
EBIT	<u>30,000</u>	<u>25,000</u>
Operating Leverage $\left( \frac{C}{EBIT} \right)$	$\frac{45,000}{30,000}$	$\frac{45,000}{25,000}$
	= 1.5	= 1.8

## (ii) Financial Leverages:

	A (₹)	B (₹)
<b>Situation I:</b>		
EBIT	30,000	30,000
Less: Interest on debt	<u>(2,000)</u>	<u>(1,000)</u>

EBT	28,000	29,000
Financial Leverage $\left(\frac{\text{EBIT}}{\text{EBT}}\right)$	$\frac{30,000}{28,000}$	$\frac{30,000}{29,000}$
	= 1.07	= 1.03
<b>Situation-II:</b>		
EBIT	25,000	25,000
Less: Interest on debt	(2,000)	(1,000)
EBT	23,000	24,000
Financial Leverage $\left(\frac{\text{EBIT}}{\text{EBT}}\right)$	$\frac{25,000}{23,000}$	$\frac{25,000}{24,000}$
	= 1.09	= 1.04

## (iii) Combined Leverages:

	A (₹)	B (₹)
(a) Situation I	$1.5 \times 1.07 = 1.61$	$1.5 \times 1.03 = 1.55$
(b) Situation II	$1.8 \times 1.09 = 1.96$	$1.8 \times 1.04 = 1.87$

## 7. Working notes

## 1 Computation of Net Present Values of Projects

Year	Cash flows		Disc. factor @ 16 %	Discounted Cash flow	
	Project A (₹)	Project B (₹)		Project A (₹)	Project B (₹)
	(1)	(2)	(3)	(3) × (1)	(3) × (2)
0	(1,35,000)	(2,40,000)	1.000	(1,35,000)	(2,40,000)
1	--	60,000	0.862	--	51,720
2	30,000	84,000	0.743	22,290	62,412
3	1,32,000	96,000	0.641	84,612	61,536
4	84,000	1,02,000	0.552	46,368	56,304
5	84,000	90,000	0.476	39,984	42,840
Net present value				58,254	34,812

## 2. Computation of Cumulative Present Values of Projects Cash inflows

Year	Project A		Project B	
	PV of cash inflows (₹)	Cumulative PV (₹)	PV of cash inflows (₹)	Cumulative PV (₹)
1	--	--	51,720	51,720
2	22,290	22,290	62,412	1,14,132
3	84,612	1,06,902	61,536	1,75,668
4	46,368	1,53,270	56,304	2,31,972
5	39,984	1,93,254	42,840	2,74,812

## (i) Discounted payback period: (Refer to Working note 2)

Cost of Project A = ₹1,35,000

Cost of Project B = ₹ 2,40,000

Cumulative PV of cash inflows of Project A after 4 years = ₹ 1,53,270

Cumulative PV of cash inflows of Project B after 5 years = ₹ 2,74,812

A comparison of projects cost with their cumulative PV clearly shows that the project A's cost will be recovered in less than 4 years and that of project B in less than 5 years. The exact duration of discounted payback period can be computed as follows:

	Project A	Project B
Excess PV of cash inflows over the project cost (₹)	18,270 (₹1,53,270 – ₹ 1,35,000)	34,812 (₹ 2,74,812 – ₹2,40,000)
Computation of period required to recover excess amount of cumulative PV over project cost (Refer to Working note 2)	0.39 year (₹ 18,270 ÷ ₹ 46,368)	0.81 years (₹34,812 ÷ ₹ 42,840)
Discounted payback period	3.61 year (4 – 0.39) years	4.19 years (5 – 0.81) years

(ii) Profitability Index: 
$$= \frac{\text{Sum of discounted cash inflows}}{\text{Initian cash outlay}}$$

Profitability Index (for Project A) = 
$$\frac{₹1,93,254}{₹1,35,000} = 1.43$$

Profitability Index (for Project B) = 
$$\frac{₹2,74,812}{₹2,40,000} = 1.15$$

(iii) Net present value (for Project A) = ₹ 58,254 (Refer to Working note 1)

Net present value (for Project B) = ₹ 34,812

8. Annual Benefit of accepting the Discount

$$\frac{₹1.5}{₹100-₹1.50} \times \frac{365 \text{ days}}{40-10 \text{ days}} = 18.53\%$$

Annual Cost = Opportunity Cost of foregoing interest on investment = 15%

If average invoice amount is ₹ 10,00,000

	If discount is	
	Accepted	Not Accepted
Payment to Supplier	9,85,000	10,00,000
Return on investment of ₹ 9,85,00 for 30 days { ₹ 9,85,000 × (30/365) × 15% }		(12,144)
	9,85,500	9,87,856

Thus, from above table it can be seen that it is cheaper to accept the discount.

9. Working Notes:

1. Raw Material Storage Period (R)

$$= \frac{\text{Average Stock of Raw Material}}{\text{Annual Consumption of Raw Material}} \times 365$$

$$= \frac{₹ 45,000 + ₹ 65,356}{2} \times 365$$

$$= \frac{₹ 3,79,644}{2} \times 365$$

$$= 53 \text{ days.}$$

Annual Consumption of Raw Material = Opening Stock + Purchases - Closing Stock

$$= ₹ 45,000 + ₹ 4,00,000 - ₹ 65,356$$

$$= ₹ 3,79,644$$

2. **Work-in-Progress (WIP) Conversion Period (W)**

$$\begin{aligned} \text{WIP Conversion Period} &= \frac{\text{Average Stock of WIP}}{\text{Annual Cost of Production}} \times 365 \\ &= \frac{\frac{\text{₹ } 35,000 + \text{₹ } 51,300}{2}}{\text{₹ } 7,50,000} \times 365 = 21 \text{ days} \end{aligned}$$

3. **Finished Stock Storage Period (F)**

$$\begin{aligned} &= \frac{\text{Average Stock of Finished Goods}}{\text{Cost of Goods Sold}} \times 365 \\ &= \frac{\text{₹ } 65,178}{\text{₹ } 9,15,000} \times 365 = 26 \text{ days.} \end{aligned}$$

$$\text{Average Stock} = \frac{\text{₹ } 60,181 + \text{₹ } 70,175}{2} = \text{₹ } 65,178.$$

4. **Debtors Collection Period (D)**

$$\begin{aligned} &= \frac{\text{Average Debtors}}{\text{Annual Credit Sales}} \times 365 \\ &= \frac{\text{₹ } 1,23,561.50}{\text{₹ } 11,00,000} \times 365 = 41 \text{ days} \end{aligned}$$

$$\text{Average debtors} = \frac{\text{₹ } 1,12,123 + \text{₹ } 1,35,000}{2} = \text{₹ } 1,23,561.50$$

5. **Creditors Payment Period (C)**

$$\begin{aligned} &= \frac{\text{Average Creditors}}{\text{Annual Net Credit Purchases}} \times 365 \\ &= \frac{\left( \frac{\text{₹ } 50,079 + \text{₹ } 70,469}{2} \right)}{\text{₹ } 4,00,000} \times 365 = 55 \text{ days} \end{aligned}$$

(i) **Operating Cycle Period**

$$\begin{aligned} &= R + W + F + D - C \\ &= 53 + 21 + 26 + 41 - 55 \\ &= 86 \text{ days} \end{aligned}$$

**(ii) Number of Operating Cycles in the Year**

$$= \frac{365}{\text{Operating Cycle Period}} = \frac{365}{86} = 4.244$$

**(iii) Amount of Working Capital Required**

$$= \frac{\text{Annual Operating Cost}}{\text{Number of Operating Cycles}} = \frac{\text{₹ } 9,50,000}{4.244} = \text{₹ } 2, 23,845.42$$

- 10 (a) "The profit maximisation is not an operationally feasible criterion." This statement is true because Profit maximisation can be a short-term objective for any organisation and cannot be its sole objective. Profit maximization fails to serve as an operational criterion for maximizing the owner's economic welfare. It fails to provide an operationally feasible measure for ranking alternative courses of action in terms of their economic efficiency. It suffers from the following limitations:
- (i) **Vague term:** The definition of the term profit is ambiguous. Does it mean short term or long term profit? Does it refer to profit before or after tax? Total profit or profit per share?
  - (ii) **Timing of Return:** The profit maximization objective does not make distinction between returns received in different time periods. It gives no consideration to the time value of money, and values benefits received today and benefits received after a period as the same.
  - (iii) It ignores the risk factor.
  - (iv) The term maximization is also vague
- (b) (i) **Bridge Finance:** Bridge finance refers, normally, to loans taken by the business, usually from commercial banks for a short period, pending disbursement of term loans by financial institutions. Normally it takes time for the financial institution to finalise procedures of creation of security, tie-up participation with other institutions etc. even though a positive appraisal of the project has been made. However, once the loans are approved in principle, firms in order not to lose further time in starting their projects arrange for bridge finance. Such temporary loan is normally repaid out of the proceeds of the principal term loans. It is secured by hypothecation of moveable assets, personal guarantees and demand promissory notes. Generally rate of interest on bridge finance is higher as compared with that on term loans.
- (ii) **Floating Rate Bonds:** These are the bonds where the interest rate is not fixed and is allowed to float depending upon the market conditions. These are ideal instruments which can be resorted to by the issuers to hedge themselves against the volatility in the interest rates. They have become more popular as a money market instrument and have been successfully issued by financial

institutions like IDBI, ICICI etc.

- (iii) **Packing Credit:** Packing credit is an advance made available by banks to an exporter. Any exporter, having at hand a firm export order placed with him by his foreign buyer on an irrevocable letter of credit opened in his favour, can approach a bank for availing of packing credit. An advance so taken by an exporter is required to be liquidated within 180 days from the date of its commencement by negotiation of export bills or receipt of export proceeds in an approved manner. Thus Packing Credit is essentially a short-term advance.
- (c) On one hand when cost of 'fixed cost fund' is less than the return on investment financial leverage will help to increase return on equity and EPS. The firm will also benefit from the saving of tax on interest on debts etc. However, when cost of debt will be more than the return it will affect return of equity and EPS unfavourably and as a result firm can be under financial distress. This is why financial leverage is known as "double edged sword".

Effect on EPS and ROE:

When,  $ROI > \text{Interest}$  – Favourable – Advantage

When,  $ROI < \text{Interest}$  – Unfavourable – Disadvantage

When,  $ROI = \text{Interest}$  – Neutral – Neither advantage nor disadvantage.



## PAPER 4: TAXATION

### SECTION A: INCOME TAX

#### PART I: STATUTORY UPDATE

The Income-tax law, as amended by the Finance Act, 2017, including significant notifications/circulars issued upto 31<sup>st</sup> October, 2017 is applicable for May, 2018 examination. The relevant assessment year for May, 2018 examination is A.Y.2018-19. The significant notifications/circulars issued upto 31.10.2017, relevant for May, 2018 examination but not covered in the July 2017 edition of the Study Material, are given hereunder.

#### CHAPTER 2: RESIDENCE AND SCOPE OF TOTAL INCOME

**Clarification regarding liability to income-tax in India of a non-resident seafarer receiving remuneration in NRE (Non-Resident External) account maintained with an Indian Bank [Circular No.13/2017, dated 11.04.2017 and Circular No.17/2017, dated 26.04.2017]**

Income by way of salary, received by non-resident seafarers, for services rendered outside India on-board foreign ships, is being subjected to tax in India for the reason that the salary has been received by the seafarer into the NRE bank account maintained in India by the seafarer. On receiving representations in this regard, the CBDT has examined the matter. It noted that section 5(2)(a) of the Income-tax Act, 1961 provides that only such income of a non-resident shall be subjected to tax in India that is either received or is deemed to be received in India.

Accordingly, the CBDT has, vide this circular, clarified that that salary accrued to a non-resident seafarer for services rendered outside India on a foreign going ship (with Indian flag or foreign flag) shall not be included in the total income merely because the said salary has been credited in the NRE account maintained with an Indian bank by the seafarer.

#### CHAPTER 4: HEADS OF INCOME UNIT IV: CAPITAL GAINS

**Long-term specified asset notified for the purpose of claiming exemption under section 54EC [Notification No. 47/2017, dated 08.06.2017 and Notification No. 79/2017, dated 08.08.2017]**

Section 54EC provides exemption from chargeability of capital gain from the transfer of a long-term capital asset where the assessee has invested the whole or any part of the capital gain in a long-term specified asset. As per clause (ba) of *Explanation* to section 54EC "long term specified asset" means any bond redeemable after three years and issued on or after 01.04.07 by the National Highways Authority of India (NHAI) or by the Rural Electrification Corporation Limited (RECL) or any other bond notified by the Central Government in this behalf.

Accordingly, the Central Government has, vide these notifications, notified any bond redeemable after three years and issued by the **Power Finance Corporation Limited** on or

after 15.06.17 or by the **Indian Railway Finance Corporation Limited** on or after 08.08.17 as 'long-term specified asset'.

**CHAPTER 4: HEADS OF INCOME  
UNIT V: INCOME FROM OTHER SOURCES**

**Clarification regarding trade advance not to be treated as deemed dividend under section 2(22)(e) – [Circular No. 19/2017, dated 12.06.2017]**

Section 2(22)(e) provides that "dividend" includes any payment by a company in which public are not substantially interested, of any sum by way of **advance or loan** to a shareholder who is the beneficial owner of shares holding not less than 10% of the voting power, or to any concern in which such shareholder is a member or a partner and in which he has a substantial interest or any payment by any such company on behalf, or for the individual benefit, of any such shareholder, to the extent to which the company in either case possesses accumulated profits.

The CBDT observed that some Courts in the recent past have held that trade advances in the nature of commercial transactions would not fall within the ambit of the provisions of section 2(22)(e) and such views have attained finality.

In view of the above, the CBDT has, vide this circular, clarified that it is a settled position that trade advances, which are in the nature of commercial transactions, would not fall within the ambit of the word 'advance' in section 2(22)(e) and therefore, the same would not to be treated as deemed dividend.

**CHAPTER 9: ADVANCE TAX AND TAX DEDUCTION AT SOURCE**

**Deduction of tax at source on interest income accrued to minor child, where both the parents have deceased [Notification No. 05/2017, dated 29.05.2017]**

Under Rule 31A(5) of the Income-tax Rules, 1962, the Director General of Income-tax (Systems) is authorized to specify the procedures, formats and standards for the purposes of furnishing and verification of, *inter alia*, the statements and shall be responsible for the day-to-day administration in relation to furnishing and verification of the statements in the manner so specified.

The Principal Director General of Income-tax (Systems) has, in exercise of the powers delegated by the CBDT under Rule 31A(5), specified that in case of minors where both the parents have deceased, TDS on the interest income accrued to the minor is required to be deducted and reported against PAN of the minor child unless a declaration is filed under Rule 37BA(2) that credit for tax deducted has to be given to another person.

**Deduction of tax at source on interest on deposits made under Capital Gains Accounts Scheme, 1988 where depositor has deceased - Notification No. 08/2017, dated 13.09.2017**

The Principal Director General of Income-tax (Systems) has, in exercise of the powers delegated by the CBDT under Rule 31A(5), vide this notification, specified that in case of deposits under the Capital Gains Accounts Scheme, 1988 where the depositor has deceased:

- (i) TDS on the interest income accrued for and upto the period of death of the depositor is required to be deducted and reported against PAN of the depositor, and
- (ii) TDS on the interest income accrued for the period after death of the depositor is required to be deducted and reported against PAN of the legal heir,

unless a declaration is filed under Rule 37BA(2) that credit for tax deducted has to be given to another person.

**No requirement to deduct tax at source under section 194-I on remittance of Passenger Service Fees (PSF) by an Airline to an Airport Operator [Circular No. 21/2017, dated 12.06.2017]**

Section 194-I requires deduction of tax at source at specified percentage on any income payable to a resident by way of rent. *Explanation* to this section defines the term “rent” as any payment, by whatever name called, under any lease, sub-lease, tenancy or any other agreement or arrangement for the use of any (a) land; or (b) building; or (c) land appurtenant to a building; or (d) machinery; (e) plant; (f) equipment (g) furniture; or (h) fitting, whether or not any or all of them are owned by the payee.

The primary requirement of any payment to qualify as rent is that the payment must be for the use of land and building and mere incidental/minor/insignificant use of the same while providing other facilities and service would not make it a payment for use of land and buildings so as to attract section 194-I.

Accordingly, the CBDT has, *vide* this circular, clarified that the provisions of section 194-I shall **not** be applicable on payment of PSF by an airline to Airport Operator.

**Clarification regarding TDS on Goods and Services Tax (GST) component comprised in payments made to residents [Circular No. 23/2017 dated 19.07.2017]**

The CBDT had, *vide* Circular No. 1/2014 dated 13.01.2014, clarified that wherever in terms of the agreement or contract between the payer and the payee, the service tax component comprised in the amount payable to a resident is indicated separately, tax shall be deducted at source on the amount paid or payable without including such service tax component.

In order to harmonize the same treatment with the new system for taxation of services under the GST regime w.e.f. 01.07.2017, the CBDT has, *vide* this circular, clarified that wherever in terms of the agreement or contract between the payer and the payee, the component of 'GST on services' comprised in the amount payable to a resident is indicated separately, tax shall be deducted at source on the amount paid or payable without including such 'GST on services' component.

GST shall include Integrated Goods and Services Tax, Central Goods and Services Tax, State Goods and Services Tax and Union Territory Goods and Services Tax.

Further, for the purposes of this Circular, any reference to “service tax” in an existing agreement or contract which was entered into prior to 01.07.2017 shall be treated as “GST on services” with respect to the period from 01.07.2017 onward till the expiry of such agreement or contract.

**CHAPTER 10: PROVISIONS FOR FILING RETURN OF INCOME****Scope of qualifications for e-Return Intermediary extended to include Company Secretaries, Cost Accountants and Tax Return Preparer [Notification No 66/2016, dated 09.08.2016]**

Section 139(1B) provides for an alternative method to furnish return of income. Vide Notification No 210/2007, dated 27.07.2007, an Electronic Furnishing of Return of Income Scheme, 2007 was notified for the said purpose. The scheme, *inter alia* provides that an eligible person may, at his option, furnish his return of income which he is required to furnish under various provisions of the Act, to an e-Return Intermediary who shall digitize the data of such return and transmit the same electronically to a server designated for this purpose by the e-Return Administrator, on or before the due date.

Para 5 of the said Notification lays down the qualifications of an e-Return Intermediary. A firm of Chartered Accountants or Advocates, which has been allotted a Permanent Account Number, as well as a Chartered Accountant or an Advocate who has been allotted a Permanent Account Number, *inter alia*, qualified to be an e-Return intermediary.

Vide this Notification, a firm of Company Secretaries or Cost Accountants, if the firm has been allotted PAN as well as a Company Secretary or a Cost Accountant or Tax Return Preparer, who has been allotted a Permanent Account Number, would also qualify to be an e-Return intermediary.

**Persons who are not required to quote Aadhar Number or Enrolment ID in application form for allotment of PAN and in return of income [Notification No. 37/2017 dated 11.05.2017]**

Section 139AA requires every person who is eligible to obtain Aadhar Number to mandatorily quote Aadhar Number or Enrolment ID of Aadhar application form, on or after 1<sup>st</sup> July, 2017 in the application form for allotment of PAN and in the return of income. However, this provision shall not applicable to such person or class or classes of persons or any State or part of any State as may be notified by the Central Government.

Accordingly, the Central Government has, vide this notification effective from 01.07.2017, notified that the provisions of section 139AA relating to quoting of Aadhar Number would not apply to an individual who does not possess the Aadhar number or Enrolment ID and is:

- (i) residing in the States of Assam, Jammu & Kashmir and Meghalaya;
- (ii) a non-resident as per Income-tax Act, 1961;
- (iii) of the age of 80 years or more at any time during the previous year;
- (iv) not a citizen of India.

**PART II: QUESTIONS AND ANSWERS****QUESTIONS**

1. Mr. Kavin, a non-resident, entered into the following transactions during the financial year 2017-18:
  - (a) Received ₹ 20 lakhs from a non-resident for use of patent for a business in India.
  - (b) Received foreign currency equivalent to ₹ 15 lakhs from a non-resident Indian for use of know-how for a business in Sri Lanka and this amount was received in Korea.
  - (c) Received ₹ 7 lakhs from RR Ltd., an Indian company as fees for providing technical services in India.
  - (d) Received ₹ 5 lakhs from R & Co., Mumbai, resident in India, for conducting the feasibility study for a new project in Nepal and the payment was made in Nepal.
  - (e) Received ₹ 8 lakhs towards interest on moneys borrowed by a non-resident for the purpose of business within India. Amount was received in Korea.

Examine briefly whether the above receipts are chargeable to tax in India.
2. Examine with reasons whether the following receipts are taxable or not under the provisions of Income-tax Act, 1961.
  - (a) Mr. Akash received a sum of ₹ 3,00,000 as compensation from “Sahayata Foundation” towards the loss of property on account of Flood Disaster at Chennai.
  - (b) Rent of ₹ 60,000 received for letting out agricultural land for a movie shooting.
  - (c) Dividend of ₹ 17 lakhs received by Mr. Yatin during P.Y. 2017-18 from A Ltd., a domestic company.
  - (d) Agricultural income of ₹ 1,30,000 of Mr. Sunil from a land situated in Canada.
3. Mr. Kashyap retired from the services of M/s ABC Ltd. on 31.01.2018, after completing service of 30 years and one month. He had joined the company on 1.1.1988 at the age of 30 years and received the following on his retirement:
  - (i) Gratuity ₹ 5,50,000. He was covered under the Payment of Gratuity Act, 1972.
  - (ii) Leave encashment of ₹ 3,30,000 for 330 days leave balance in his account. He was credited 30 days leave for each completed year of service.
  - (iii) As per the scheme of the company, he was offered a car on 31.01.2018 which was purchased on 01.03.2015 by the company for ₹ 5,00,000. Company has recovered ₹ 2,00,000 from him for the car. Company depreciates the vehicles at the rate of 15% on Straight Line Method.
  - (iv) An amount of ₹ 3,00,000 as commutation of pension for 2/3 of his pension commutation.

(v) Company presented him a gift voucher worth ₹ 8,000 on his retirement.

Following are the other particulars:

- (i) He has drawn a basic salary of ₹ 20,000 and dearness allowance @50% of basic salary for the period from 01.04.2017 to 31.01.2018. Dearness allowance does not form part of pay for retirement benefits.
- (ii) Received pension of ₹ 7,000 per month for the period 01.02.2018 to 31.03.2018 after commutation of pension.

Compute his income taxable under the head "Salaries" for Assessment Year 2018-19.

4. In August 2016, Mr. Kailash, a first-time home buyer, borrowed a sum of ₹ 35 lakhs from the National Housing Bank for construction of a residential house for ₹ 48 lakhs. The loan was sanctioned on 12.5.2016. The loan amount was disbursed directly to the flat promoter by the bank. The construction was completed in May, 2018 and repayments towards principal and interest commenced immediately after disbursement of loan.

In the light of the above facts, examine:

- (i) Whether Mr. Kailash can claim deduction under section 24 in respect of interest for the A.Y. 2018-19?
- (ii) Whether deduction under Section 80C and 80EE can be claimed by him for the A.Y. 2018-19?
5. Mr. Abhay has furnished the following particulars relating to payments made and expenditure incurred towards scientific research for the year ended 31.3.2018:

Sl. No.	Particulars	₹ (in lakhs)
(i)	Payments made to an approved Agro Research Association	25
(ii)	Payment made to RR University, an approved University	15
(iii)	Payment made to XY College	17
(iv)	Payment made to IIT, Madras (under an approved programme for scientific research)	10
(v)	Machinery purchased for in-house scientific research	20
(vi)	Salaries to research staff engaged in in-house scientific research	14

Compute the deduction available under section 35 of the Income-tax Act, 1961 for A.Y. 2018-19, while determining his income under the head "Profits and gains of business or profession".

6. Mr. Arjun bought a vacant land for ₹ 80 lakhs in March 2005. Registration and other expenses were 10% of the cost of land. He constructed a residential building on the said land for ₹ 100 lakhs during the financial year 2006-07.

He entered into an agreement for sale of the above said residential house with Mr. Jerry (not a relative) on 9<sup>th</sup> April 2017 and received ₹ 20 lakhs as advance in cash on that date. The stamp duty value on that date was ₹ 740 lakhs. The actual sale consideration was, however, fixed at ₹ 700 lakhs.

The sale deed was executed and registered on 10-6-2017 for the agreed consideration. However, the State stamp valuation authority had revised the values, hence, the value of property for stamp duty purposes was ₹ 770 lakhs on the date registration. Mr. Arjun paid 1% as brokerage on sale consideration received.

Subsequent to sale, Mr. Arjun made following investments:

- (i) Acquired a residential house at Mumbai for ₹ 110 lakhs.
- (ii) Acquired a residential house at London for ₹ 150 lakhs.
- (iii) Subscribed to NHAI bond: ₹ 45 lakhs on 29-8-2017 and ₹ 50 lakhs on 12-10-2017.

Compute the income chargeable under the head “Capital Gains” for A.Y. 2018-19. The choice of exemption must be in the manner most beneficial to the assessee.

Cost Inflation Index:	F.Y. 2004-05	113
	F.Y. 2006-07	122
	F.Y. 2017-18	272

7. From the following transactions relating to Mrs. Sonu, determine the amount chargeable to tax in her hands for the A.Y. 2018-19. Your answer should be supported by reasons:
- (i) Received cash gifts on the occasion of her marriage on 19-11-2017 of ₹ 2,10,000. It includes gift of ₹ 55,000 received from non-relatives.
  - (ii) On 1-1-2018, being her birthday, she received a gift of ₹ 45,000 by means of cheque from her father's maternal uncle.
  - (iii) On 12-2-2018, she acquired a vacant site from her friend for ₹ 1,12,000. The State stamp valuation authority fixed the value of site at ₹ 1,92,000 for stamp duty purpose.
  - (iv) She bought 50 equity shares of a private company from another friend for ₹ 75,000. The fair market value of such shares on the date of purchase was ₹ 1,33,000.
8. Compute the income to be included in the hands of Mr. Sharma for the Assessment year 2018-19 with reasons from the following information:

A proprietary business was started by Mrs. Sharma in the year 2015. As on 1.4.2016 her capital in business was ₹ 5,00,000. Her husband gifted ₹ 3,00,000 on 2.4.2016, which Mrs. Sharma

invested in her business on the same date. Mrs. Sharma earned profits from her proprietary business for the financial year 2016-17, ₹ 2,00,000 and financial year 2017-18 ₹ 4,20,000.

9. The following are the details relating to Mr. Gupta, a resident Indian, relating to the year ended 31.3.2018:

Particulars	₹
Income from salaries	2,20,000
Long-term capital loss from sale of listed shares in recognized stock exchange (STT paid at the time of sale and acquisition of shares)	1,50,000
Loss from cloth business	2,40,000
Income from speculation business	30,000
Loss from specified business covered by section 35AD	45,000
Long-term capital gains from sale of urban land	2,50,000
Loss from house property	2,50,000
Loss from card games	40,000
Income from betting (Gross)	35,000
Life Insurance Premium paid (Sum assured ₹ 5,00,000)	25,000

Compute his total income for A.Y. 2018-19 and show the items eligible for carry forward.

10. For the A.Y. 2018-19, the Gross Total Income of Mr. Raja, a resident in India, was ₹ 8,00,000 which includes long-term capital gain of ₹ 2,50,000 and Short-term capital gain of ₹ 50,000. The Gross Total Income also includes interest income of ₹ 15,000 from savings bank deposits with banks. Mr. Raja has invested in PPF ₹ 1,40,000 and also paid a medical insurance premium ₹ 35,000 for self. Mr. Raja also contributed ₹ 50,000 to Public Charitable Trust eligible for deduction under section 80G by way of an account payee cheque. Compute the total income and tax thereon of Mr. Raja, who is 65 years old as on 31.3.2018.
11. Mr. Yusuf Khan, a resident individual aged 55, furnishes the following information pertaining to the year ended 31.3.2018:
- (i) He is a working partner in ABC & Co. He has received the following amounts from the firm:
- Interest on capital at 15% : ₹ 3,00,000
- Salary as working partner (at 1% of firm's sales) (allowed fully to the firm): ₹ 90,000
- (ii) He is engaged in a business of manufacturing. The Profit and Loss account pertaining to this proprietary business (summarised form) is as under:



Particulars	₹	Particulars	₹
To Salaries	1,20,000	By Gross profit	12,50,000
To Bonus	48,000	By Interest on Bank FD (Net of TDS)	45,000
To Car expenses	50,000	By Agricultural income	60,000
To Machinery repairs	2,34,000	By Pension from LIC Jeevan Dhara	24,000
To Advance tax	70,000		
To Depreciation on:			
- Car	3,00,000		
- Machinery	1,25,000		
To Net profit	<u>4,32,000</u>		
	<b><u>13,79,000</u></b>		<b><u>13,79,000</u></b>

**Details of assets:**

Particulars	₹
<b>Opening WDV of assets are as under:</b>	
Car	3,00,000
Machinery (Used during the year for 179 days)	6,50,000
<b>Additions to machinery:</b>	
Purchased on 23.9.2017 by cash in single payment	2,00,000
Purchased on 12.11.2017 by account payee cheque	3,00,000
Second hand machinery purchased on 12.4.2017 by bearer cheque in single payment	1,25,000

(All assets added during the year were put to use immediately after purchase)

One-fifth of the car expenses are towards estimated personal use of the assessee.

Salary includes ₹ 15,000 paid by way of a single cash payment to manager.

- (iii) In February, 2016, he had sold a house at Chennai. Arrears of rent relating to this house amounting to ₹ 75,000 was received in March, 2018.
- (iv) Details of his Savings and Investments are as under:

Particulars	₹
Life insurance premium for policy in the name of his major son employed in a multinational company, at a salary of ₹ 10 lakhs p.a. (Sum assured ₹ 2,00,000) (Policy taken on 1.07.2013)	30,000
Contribution to PPF	70,000

Medical Insurance premium for his father aged 79, who is not dependent on him	32,000
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You are required to compute the total income of Mr. Yusuf Khan for the assessment year 2018-19.

12. Mr. Sachal, a resident individual aged 54, furnishes his income & other details for the P.Y. 2017-18:
- Income of ₹ 8,10,000 from wholesale cloth business, whose accounts are audited u/s 44AB.
  - Income from other sources ₹ 2,70,000.
  - Tax deducted at source ₹ 25,000.
  - Advance tax paid ₹ 1,03,000 during the P.Y. 2017-18.

Return of income filed on 11-12-2018. Calculate the interest payable under section 234B of the Income-tax Act, 1961. Assume that the return of income would be processed on the same day of filing of return. What are the consequences for delay in furnishing return of income under the Income-tax Act, 1961? Examine, making the required computations in this case.

13. Ms. Geetha submits her return of income on 29-09-2018 for A.Y 2018-19 consisting of income under the head "Salaries", "Income from house property" and bank interest. On 01-02-2019, she realized that she had not claimed deduction under section 80D in respect of medical insurance premium of ₹ 15,000 paid for her mother. She wants to revise her return of income. Can she do so? Examine.

Would your answer be different if she discovered this omission on 02-04-2019?

#### SUGGESTED ANSWERS

1. **Taxability of certain receipts in the hands of Mr. Kavin, a non-resident, for A.Y. 2018-19**

	Taxability	Reason
(a)	<b>Taxable</b>	Amount of ₹ 20 lakhs received from a non-resident is deemed to accrue or arise in India by virtue of section 9(1)(vi)(c), since the patent was used for a business in India. Therefore, the amount is chargeable to tax in India.
(b)	<b>Not Taxable</b>	Foreign currency equivalent to ₹ 15 lakhs received in Korea from a non-resident for use of know-how for a business in Sri Lanka is not deemed to accrue or arise in India as per section 9(1)(vi)(c), since it is in respect of a business carried on outside India. Also, the amount was received outside India. Therefore, the same is not chargeable to tax in India.

(c)	<b>Taxable</b>	Amount of ₹ 7 lakhs received from RR Ltd., an Indian Company, is deemed to accrue or arise in India by virtue of section 9(1)(vii)(b), since it is for providing technical services in India. Therefore, the same is chargeable to tax in India.
(d)	<b>Not Taxable</b>	Amount of ₹ 5 lakhs received in Nepal from R & Co., a resident, for conducting feasibility study for the new project in Nepal is not deemed to accrue or arise in India as per section 9(1)(vii)(b), since such study was done for a project outside India. The amount was also received outside India. Therefore, the same is not chargeable to tax in India.
(e)	<b>Taxable</b>	Amount of ₹ 8 lakhs received in Korea towards interest on moneys borrowed by a non-resident for the purpose of business within India is deemed to accrue or arise in India by virtue of section 9(v)(c), since money borrowed was used for the purpose of business in India. Therefore, the same is chargeable to tax in India.

2. **Taxability of receipts under the provisions of Income-tax Act, 1961**

	<b>Taxable/ Not taxable</b>	<b>Reason</b>
(a)	Taxable	As per section 10(10BC), any amount received or receivable by an individual as compensation, on account of any disaster, from the Central Government, State Government or a local authority is exempt from tax, to the extent the individual has not been allowed deduction under any other provision of Income-tax Act, 1961 on account of any loss or damage caused by such disaster. However, in this case, since Mr., Akash has received a compensation of ₹ 3,00,000 from Sahayata Foundation, and not from the Central Government or State Government or local authority, no exemption will be available under section 10(10BC) and the same is chargeable to tax.
(b)	Taxable	Agricultural income is exempt from income-tax as per section 10(1). Agriculture income means, <i>inter alia</i> , any rent or revenue derived from land which is situated in India and is used for agricultural purposes. In this case, rent is being derived from letting out of agricultural land for a movie shoot, which is not an agricultural purpose. In effect, the land is not being put to use for agricultural purposes. Therefore, ₹ 60,000, being rent received from letting out agricultural land for movie shooting, is not exempt under section 10(1) and the same is chargeable to tax.

(c)	Partly taxable	<p>Dividend received from a domestic company is subject to dividend distribution tax in the hands of domestic company under section 115-O.</p> <p>Dividend income received from an Indian company, which is subject to dividend distribution tax, is exempt under section 10(34). However, dividend in excess of ₹ 10 lakhs received, <i>inter alia</i>, by an individual is chargeable to tax under section 115BBDA and not exempt under section 10(34).</p> <p>Therefore, in this case, dividend received upto ₹ 10 lakh is exempt in the hands of Mr. Yatin under section 10(34). ₹ 7 lakh, being dividend in excess of ₹ 10 lakh, is taxable in his hands @10% as per section 115BBDA.</p>
(d)	Taxable	<p>Agricultural income from a land situated in any foreign country is not exempt under section 10(1) and hence, is chargeable to tax.</p> <p>Therefore, in this case, agricultural income of ₹ 1,30,000 of Mr. Sunil from land situated in Canada is taxable.</p>

3. Computation of income chargeable under the head "Salaries" of Mr. Kashyap for A.Y. 2018-19

Particulars	₹
Basic Salary = ₹ 20,000 x 10	2,00,000
Dearness Allowance = 50% of basic salary	1,00,000
Gift Voucher (See Note - 1)	8,000
Transfer of car (See Note - 2)	1,20,000
Gratuity (See Note - 3)	30,769
Leave encashment (See Note - 4)	1,30,000
Uncommuted pension (₹ 7000 x 2)	14,000
Commuted pension (See Note - 5)	<u>1,50,000</u>
<b>Taxable Salary /Gross Total Income</b>	<b><u>7,52,769</u></b>

**Notes:**

- (1) As per Rule 3(7)(iv), the value of any gift or voucher or token in lieu of gift received by the employee or by member of his household not exceeding ₹ 5,000 in aggregate during the previous year is exempt. In this case, the amount was received on his retirement and the sum exceeds the limit of ₹ 5,000.

Therefore, the entire amount of ₹ 8,000 is liable to tax as perquisite.

**Note** - An alternate view is possible that only the sum in excess of ₹5,000 is taxable in view of the language of Circular No.15/2001 dated 12.12.2001. Gifts upto ₹5,000 in the aggregate per annum would be exempt, beyond which it would be taxed as a perquisite. As per this view, the value of perquisite would be ₹3,000 and gross total income would be ₹7,47,769.

- (2) **Perquisite value of transfer of car:** As per Rule 3(7)(viii), the value of benefit to the employee arising from the transfer of an asset, being a motor car, by the employer is the actual cost of the motor car to the employer as reduced by 20% on a written down value basis for each completed year during which such motor car was put to use by the employer. Therefore, the value of perquisite on transfer of motor car, in this case, would be:

Particulars	₹
Purchase price (1.3.2015)	5,00,000
Less: Depreciation @ 20%	<u>1,00,000</u>
WDV on 29.2.2016	4,00,000
Less: Depreciation @ 20%	<u>80,000</u>
WDV on 28.2.2017	3,20,000
Less: Amount recovered	<u>2,00,000</u>
<b>Value of perquisite</b>	<b><u>1,20,000</u></b>

Under Rule 3(7)(viii), while calculating the perquisite value of benefit to the employee arising from the transfer of any movable asset, the normal wear and tear is to be calculated in respect of each completed year during which the asset was put to use by the employer. In the given case, the third year of use of car is completed on 28.2.2018 whereas the car was sold to the employee on 31.1.2018. Accordingly, wear and tear has to be calculated @20% on reducing balance method for only two years.

The rate of 15% as well as the straight line method adopted by the company for depreciation of vehicle is not relevant for calculation of perquisite value of car in the hands of Mr. Kashyap.

- (3) **Taxable gratuity**

Particulars	₹
Gratuity received	5,50,000
Less: Exempt under section 10(10) - Least of the following:	
(i) Notified limit = ₹ 10,00,000	
(ii) Actual gratuity received = ₹ 5,50,000	

(iii) $15/26 \times$ last drawn salary $\times$ no. of completed years or part in excess of 6 months $15/26 \times 30,000 \times 30 = ₹ 5,19,231$	<u>5,19,231</u>
<b>Taxable Gratuity</b>	<b><u>30,769</u></b>

**Note** – As per the Payment of Gratuity Act, 1972, dearness allowance is included in the meaning of salary. Since, in this case, Mr. Kashyap is covered under the Payment of Gratuity Act, 1972, dearness allowance has to be included within the meaning of salary for computation of exemption under section 10(10).

(4) **Taxable leave encashment**

Particulars	₹
Leave Salary received	3,30,000
Less: Exempt under section 10(10AA) - Least of the following:	
(i) Notified limit	₹ 3,00,000
(ii) Actual leave salary received	₹ 3,30,000
(iii) 10 months $\times$ ₹ 20,000	₹ 2,00,000
(iv) Cash equivalent of leave to his credit	₹ 2,20,000
$\left( \frac{330}{30} \times 20,000 \right)$	<u>2,00,000</u>
<b>Taxable Leave encashment</b>	<b><u>1,30,000</u></b>

**Note** - Salary, for the purpose of exemption under section 10(10AA), would include dearness allowance only if it forms part of pay for retirement benefits. Therefore, in this case, since dearness allowance does not form part of pay for retirement benefits, only basic salary has to be considered for computing exemption under section 10(10AA).

(5) **Commuted Pension**

Since Mr. Kashyap is a non-government employee in receipt of gratuity, exemption under section 10(10A) would be available to the extent of  $1/3^{\text{rd}}$  of the amount of the commuted pension which he would have received had he commuted the whole of the pension.

Particulars	₹
Amount received	3,00,000
Less: Exemption under section 10(10A) = $\frac{1}{3} \times \left[ 3,00,000 \times \frac{3}{2} \right]$	<u>1,50,000</u>
<b>Taxable amount</b>	<b><u>1,50,000</u></b>

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

It is stated that the construction is completed only in May, 2018. Hence, deduction under section 24 in respect of interest on housing loan cannot be claimed in the assessment year 2018-19.

**(ii) Deduction under section 80C cannot be claimed**

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

However, deduction is *prima facie* eligible only if the income from such property is chargeable to tax under the head "Income from House Property". During the assessment year 2018-19, there is no such income chargeable under this head. Hence, deduction under section 80C cannot be claimed for A.Y. 2018-19.

**Deduction under section 80EE can be claimed**

As per section 80EE, interest payable on loan taken for the purpose of acquisition of a residential house from any financial institution qualifies for deduction, subject to a maximum of ₹ 50,000, provided following conditions are satisfied –

- (i) Such loan is sanctioned during the P.Y. 2016-17
- (ii) The value of the house does not exceed ₹ 50 lakhs
- (iii) The amount of loan sanctioned does not exceed ₹ 35 lakhs and
- (iv) the assessee does not own any residential house on the date of sanction of loan

Section 80EE does not pose any restriction regarding the chargeability of the income from such property under the head "Income from House Property. Therefore, in this case, since Mr. Kailash satisfies all the conditions stipulated under section 80EE, interest on such loan would qualify for deduction under section 80EE, subject to a maximum of ₹ 50,000.

## 5. Computation of deduction allowable under section 35

Particulars	Amount (₹ in lakhs)	Section	% of weighted deduction	Amount of deduction (₹ in lakhs)
<b>Payment for scientific research</b>				
Approved Agro Research Association	25	35(1)(ii)	150%	37.5
RR University, an approved University	15	35(1)(ii)	150%	22.5
XY College [See Note 1]	17	-	NIL	NIL
IIT Madras (under an approved programme for scientific research)	10	35(2AA)	150%	15
<b>In-house research [See Note 2]</b>				
Capital expenditure – Purchase of Machinery	20	35(1)(iv) r. w. 35(2)	100%	20
Revenue expenditure - Salaries to research staff engaged in in-house scientific research	14	35(1)(i)	100%	<u>14</u>
<b>Deduction allowable under section 35</b>				<b><u>109</u></b>

**Notes:-**

- 1. Payment to XY College:** Since the question clearly mentions that only Agro Research Association and RR University (mentioned in item (i) and (ii), respectively) are approved research institutions, it is logical to conclude that XY College mentioned in item (iii) is not an approved research institution. Therefore, payment to XY College would not qualify for deduction under section 35.
- 2. Deduction for in-house research and development:** Only company assessee are entitled to weighted deduction @150% under section 35(2AB) in respect of expenditure on scientific research on in-house research and development facility. However, in this case, the assessee is an individual. Therefore, he would be entitled to deduction@100% of the revenue expenditure incurred under section 35(1)(i) and 100% of the capital expenditure incurred under section 35(1)(iv) read with section 35(2), assuming that such expenditure is laid out or expended on scientific research related to his business.



## 6. Computation of income chargeable under the head “Capital Gains” for A.Y.2018-19

Particulars	₹ (in lakhs)	₹ (in lakhs)
<b>Capital Gains on sale of residential building</b>		
Actual sale consideration ₹ 700 lakhs		
Value adopted by Stamp Valuation Authority ₹ 770 lakhs		
Gross Sale consideration		770.00
[In case the actual sale consideration declared by the assessee is less than the value adopted by the Stamp Valuation Authority for the purpose of charging stamp duty, then, the value adopted by the Stamp Valuation Authority shall be taken to be the full value of consideration as per section 50C.		
In a case where the date of agreement is different from the date of registration, stamp duty value on the date of agreement can be considered provided the whole or part of the consideration is paid by way of account payee cheque/bank draft or by way of ECS through bank account on or before the date of agreement. In this case, since advance of ₹ 20 lakh is paid by cash, stamp duty value of ₹ 740 lakhs on the date of agreement cannot be adopted as the full value of consideration. Stamp duty value on the date of registration would be the full value of consideration]		
<b>Less: Brokerage@1% of sale consideration (1% of ₹ 700 lakhs)</b>		<u>7.00</u>
<b>Net Sale consideration</b>		763.00
<b>Less: Indexed cost of acquisition</b>		
- Cost of vacant land, ₹ 80 lakhs, plus registration and other expenses i.e., ₹ 8 lakhs, being 10% of cost of land [₹ 88 lakhs × 272/113]	211.82	
- Construction cost of residential building (₹ 100 lakhs × 272/122)	<u>222.95</u>	
		<u>434.77</u>
<b>Long-term capital gains before exemption</b>		<b>328.23</b>
<b>Less: Exemption under section 54</b>		110.00
The capital gain arising on transfer of a long-term residential property shall not be chargeable to tax to the extent such capital gain is invested in the purchase of one residential house property in India one year before or two years after the date of transfer of original asset.		
Therefore, in the present case, the exemption would be available only in respect of the residential house acquired at Mumbai and not in respect of the residential house in London		

<b>Less: Exemption under section 54EC</b>	50.00
Amount deposited in capital gains bonds of NHAI within six months from the date of transfer (i.e., on or before 09.12.2017) would qualify for exemption, to the maximum extent of ₹ 50 lakhs. Therefore, in the present case, exemption can be availed only to the extent of ₹ 50 lakh out of ₹ 95 lakhs, even if the both the investments are made on or before 09.12.2017 (i.e., within six months from the date of transfer).	
<b>Long term capital gains chargeable to tax</b>	<b>168.23</b>

**Note:** Since the residential house property was held by Mr. Arjun for more than 24 months immediately preceding the date of its transfer, the resultant gain is a long-term capital gain.

**7. Computation of amount chargeable to tax in hands of Mrs. Sonu for A.Y. 2018-19**

	Particulars	₹
(i)	Cash gift of ₹ 2,10,000 received on the occasion of her marriage is not taxable, since gifts received by an individual on the occasion of marriage is excluded from tax under section 56(2)(x), even if the same are from non-relatives.	Nil
(ii)	Even though father's maternal uncle does not fall within the definition of "relative" under section 56(2)(x), gift of ₹ 45,000 received from him by cheque is not chargeable to tax since the aggregate sum of money received by Mrs. Sonu without consideration from non-relatives (other than on the occasion of marriage) during the previous year 2017-18 does not exceed ₹ 50,000.	Nil
(iii)	Purchase of vacant site for inadequate consideration on 12.2.2018 would attract the provisions of section 56(2)(x). Where any immovable property is received for a consideration which is less than the stamp duty value of the property by an amount exceeding ₹ 50,000, the difference between the stamp duty value and consideration is chargeable to tax in the hands of Individual. Therefore, in the given case ₹ 80,000 (₹ 1,92,000 - ₹ 1,12,000) is taxable in the hands of Mrs. Sonu.	80,000
(iv)	Since shares are included in the definition of "property" and difference between the purchase value and fair market value of shares is ₹ 58,000 (₹ 1,33,000 - ₹ 75,000) i.e. it exceeds ₹ 50,000, the difference would be taxable under section 56(2)(x).	58,000
	<b>Amount chargeable to tax</b>	<b>1,38,000</b>

8. Section 64(1)(iv) provides for the clubbing of income in the hands of the individual, if the income earned is from the assets 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, Mrs. Sharma received a gift of ₹ 3,00,000 from her husband which she invested in her business. In a case where gift from spouse has been invested in business, as per *Explanation 3* to section 64(1), the income or loss from such business for any previous year has to be apportioned between the spouses on the basis of the ratio of their capital employed as on 1<sup>st</sup> April of the relevant previous year. Accordingly, the income to be included in the hands of Mr. Sharma for A.Y.2018-19 has to be computed as under:

Particulars	Mrs. Sharma's Capital Contribution	Capital Contribution Out of gift from husband	Total
	₹	₹	₹
Capital as on 1.4.2016	5,00,000	--	5,00,000
Investment on 02.04.2016 out of gift received from her husband		3,00,000	3,00,000
	5,00,000	3,00,000	8,00,000
Profit for F.Y. 2016-17 to be apportioned on the basis of capital employed on the first day of the P.Y. i.e., on 1.4.2016	2,00,000		2,00,000
<b>Capital employed as on 1.4.2017</b>	<b>7,00,000</b>	<b>3,00,000</b>	<b>10,00,000</b>
Profit for F.Y. 2017-18 to be apportioned on the basis of capital employed as on 1.4.2017 (i.e., 7:3)	2,94,000	1,26,000	4,20,000

Therefore, the income to be included in the hands of Mr. Sharma for A.Y.2018-19 is ₹ 1,26,000.

9. **Computation of total income of Mr. Gupta for the A.Y.2018-19**

Particulars	₹	₹
<b>Salaries</b>		
Income from salaries	2,20,000	
Less: Loss from house property [See Note (i)]	<u>2,00,000</u>	20,000

<b>Profits and gains of business or profession</b>		
Income from speculation business	30,000	
Less: Loss from cloth business set off [See Note (iv)]	<u>30,000</u>	Nil
<b>Capital gains</b>		
Long-term capital gains from sale of urban land	2,50,000	
Less: Loss from cloth business set off [See Note (iv)]	<u>2,10,000</u>	40,000
<b>Income from other sources</b>		
Income from betting		<u>35,000</u>
<b>Gross Total Income</b>		<b>95,000</b>
Less: Deduction under section 80C (life insurance premium paid) [See Note (vi)]		<u>20,000</u>
<b>Total income</b>		<b><u>75,000</u></b>

**Losses to be carried forward:**

Particulars		₹
(1)	Loss from house property (₹ 2,50,000 - ₹ 2,00,000)	50,000
(2)	Loss from cloth business (₹ 2,40,000 - ₹ 30,000 - ₹ 2,10,000)	Nil
(3)	Loss from specified business covered by section 35AD	45,000

**Notes:**

- (i) As per section 71(3A), loss from house property can be set-off against income under any other head to the extent of ₹ 2,00,000 only. As per section 71B, balance loss not set-off can be carried forward to the next year for set-off against income from house property of that year.
- (ii) Long-term capital gains from sale of listed shares in a recognized stock exchange on which STT is paid at the time of acquisition and sale is exempt under section 10(38). Loss from an exempt source cannot be set off against profits from a taxable source. Therefore, long-term capital loss on sale of listed shares on which STT is paid cannot be set-off against long-term capital gains from sale of urban land. Such loss cannot also be carried forward for set-off in the subsequent years.
- (iii) Loss from specified business covered by section 35AD can be set-off only against profits and gains of any other specified business. Therefore, such loss cannot be set off against any other income. The unabsorbed loss has to be carried forward for set-off against profits and gains of any specified business in the following year(s).
- (iv) Since inter-source set-off of losses is permissible as per section 70(1), loss from cloth business to the extent of ₹ 30,000 can be set-off against income from speculation business. The remaining business loss cannot be set off against salary income due

to restriction contained in section 71(2A). However, the remaining business loss of ₹ 2,10,000 (₹ 2,40,000 – ₹ 30,000) can be set-off against long-term capital gains of ₹ 2,50,000 from sale of urban land. Consequently, the taxable long-term capital gains would be ₹ 40,000.

- (v) Loss from card games can neither be set off against any other income, nor can it be carried forward.
- (vi) For providing deduction under Chapter VI-A, gross total income has to be reduced by the amount of long-term capital gains and casual income. Therefore, the deduction under section 80C in respect of life insurance premium paid has to be restricted to ₹ 20,000 [i.e., Gross Total Income of ₹ 1,05,000 – ₹ 40,000 (LTCG) – ₹ 45,000 (Casual income)].
- (vii) Income from betting is chargeable to tax at a flat rate of 30% under section 115BB and no expenditure or allowance can be allowed as deduction from such income, nor can any loss be set-off against such income.

**10. Computation of total income and tax payable by Mr. Raja for the A.Y. 2018-19**

Particulars	₹	₹
Gross total income including long term capital gain		8,00,000
Less: Long term capital gain		<u>2,50,000</u>
		5,50,000
<b>Less: Deductions under Chapter VI-A:</b>		
<b>Under section 80C</b> in respect of PPF deposit	1,40,000	
<b>Under section 80D</b> (it is assumed that premium of ₹ 35,000 is paid by otherwise than by cash. The deduction would be restricted to ₹ 30,000, since Mr. Raja is a resident senior citizen)	30,000	
<b>Under section 80G</b> (See Notes 1 & 2 below)	18,500	
<b>Under section 80TTA</b> (See Note 3 below)	<u>10,000</u>	<u>1,98,500</u>
<b>Total income (excluding long term capital gains)</b>		<b><u>3,51,500</u></b>
<b>Total income (including long term capital gains)</b>		<b>6,01,500</b>
Tax on total income (including long-term capital gains of ₹ 2,50,000)		
LTCG ₹ 2,50,000 x 20%		50,000
Balance total income ₹ 3,51,500: Tax @5% on ₹ 51,500 (₹ 3,51,500 – ₹ 3,00,000, being the basic exemption limit for senior citizen)		<u>2,575</u>
		<u>52,575</u>

Add: Education cess @2% and Secondary and higher education cess @1%		<u>1,577</u>
<b>Total tax liability</b>		<b><u>54,152</u></b>
<b>Total tax liability (rounded off)</b>		<b>54,150</b>

**Notes:****1. Computation of deduction under section 80G:**

Particulars	₹
Gross total income (excluding long term capital gains)	5,50,000
Less: Deduction under section 80C, 80D & 80TTA	1,80,000
	<b><u>3,70,000</u></b>
10% of the above	37,000
Contribution made to Public Charitable Trust	50,000
Lower of the two eligible for deduction under section 80G	37,000
<b>Deduction under section 80G – 50% of ₹ 37,000</b>	<b>18,500</b>

2. Deduction under section 80G is allowed only if amount is paid by any mode other than cash, in case of amount exceeding ₹ 2,000. Therefore, the contribution made to public charitable trust is eligible for deduction since it is made by way of an account payee cheque.
3. Deduction of upto ₹ 10,000 under section 80TTA is allowed, *inter alia*, to an individual assessee if gross total income includes interest income from deposits in a saving account with bank. Since Gross Total Income of Mr. Raja includes interest income of ₹ 15,000 on savings bank deposit, he is eligible for deduction of ₹ 10,000 under section 80TTA.

**11. Computation of total income of Mr. Yusuf Khan for the A.Y. 2018-19**

Particulars	₹	₹
<b>Income from house property</b>		
Arrears of rent received in respect of the Chennai house taxable under section 25A [Note 1]	75,000	
Less: Deduction @ 30%	<u>22,500</u>	52,500
<b>Profits and gains of business or profession</b>		
(a) Own business [Note 3]		6,37,000
(b) Income from partnership firm [Note 2]		
Interest on capital	2,40,000	

[As per section 28(v), chargeable in the hands of the partner only to the extent allowable as deduction in the firm's hand i.e. @12%] Salary of working partner (Since the same has been fully allowed as deduction in the hands of the firm)		<u>90,000</u>	3,30,000
<b>Income from other sources</b>			
(a) LIC Jeevan Dhara pension		24,000	
(b) Interest from bank FD (gross)		<u>50,000</u>	<u>74,000</u>
<b>Gross Total Income</b>			<b>10,93,500</b>
<i>Less: Deductions under Chapter VIA</i>			
<b>Section 80C</b>			
Life insurance premium for policy in the name of major son qualifies for deduction even though he is not dependent on the assessee. However, the same has to be restricted to 10% of sum assured i.e. 10% of ₹ 2,00,000.	20,000		
Contribution to PPF	<u>70,000</u>	90,000	
<b>Section 80D</b>			
Mediclaim premium for father, a senior citizen (qualifies for deduction, even though the father is not dependent on the assessee, subject to a maximum of ₹ 30,000)	32,000	<u>30,000</u>	<u>1,20,000</u>
<b>Total Income</b>			<b><u>9,73,500</u></b>

**Notes:**

- (1) As per section 25A, any arrears of rent received will be chargeable to tax, after deducting a sum equal to 30% of such arrears, as income from house property in the year of receipt, whether or not the assessee is the owner of the house property.
- (2) The income by way of interest on capital and salary of Mr. Yusuf Khan from the firm, ABC & Co., in which he is a working partner, to the extent allowed as deduction in the hands of the firm under section 40(b), has to be included in the business income of the partner as per section 28(v). Accordingly, ₹ 3,30,000 [i.e., ₹ 90,000 (salary) + ₹ 2,40,000 (interest@12%)] should be included in his business income.
- (3) **Computation of income from own business**

Particulars	₹	₹
Net profit as per profit and loss account		4,32,000

Less: Items credited to profit and loss account not treated as business income		
Interest on bank FD (Net of TDS)	45,000	
Agricultural income	60,000	
Pension from LIC Jeevan Dhara	<u>24,000</u>	<u>1,29,000</u>
		3,03,000
Add: Items debited to profit and loss account to be disallowed/considered separately		
Advance tax	70,000	
Depreciation:		
- Car	3,00,000	
- Machinery	1,25,000	
Car expenses disallowed for personal use (₹ 50,000 x 1/5)	10,000	
Salary to manager disallowed under section 40A(3) since it is paid in cash and the same exceeds ₹ 10,000	<u>15,000</u>	<u>5,20,000</u>
		<b>8,23,000</b>
Less: Depreciation (See Working Note below)		<u>1,86,000</u>
<b>Income from business</b>		<b><u>6,37,000</u></b>

**Working Note:****Computation of depreciation allowable under the income-tax Act, 1961**

Particulars	₹	₹
<b>On Car:</b>		
Depreciation @15% on 3,00,000	45,000	
Less: 1/5 <sup>th</sup> for personal use	<u>9,000</u>	
<b>Depreciation on Car allowable as deduction</b>		<b>36,000</b>
<b>On Machinery:</b>		
Opening WDV	6,50,000	
Additions during the year (used for more than 180 days)		
- New Machinery purchased on 23.9.17	2,00,000	
- Second hand machinery purchased on 12.4.17	1,25,000	
Additions during the year (used for less than 180 days)	3,00,000	



<b>Normal Depreciation</b>		
Depreciation @15% on ₹ 6,50,000	97,500	
[As per second proviso to section 43(1), the expenditure for acquisition of asset, in respect of which payment to a person in a day exceeds ₹10,000 has to be ignored for computing actual cost, if such payment is made otherwise than by way of A/c payee cheque/ bank draft or ECS. Accordingly, depreciation on second hand machinery purchased on 12.4.2017 and on new machinery purchased on 23.9.2017 is not allowable since the payment is made otherwise than by A/c payee cheque/A/c payee draft/ ECS to a person in a day]		
Depreciation @ 7.5% on ₹ 3,00,000	<u>22,500</u>	
<b>Total normal depreciation on machinery (A)</b>	<b>1,20,000</b>	
Where an asset acquired during the year is put to use for less than 180 days, 50% of the rate of depreciation is allowable. This restriction does not apply to assets acquired in an earlier year.		
<b>Additional depreciation (B)</b>		
New machinery		
Used for less than 180 days = 10% of ₹ 3,00,000	<u>30,000</u>	
<b>Total permissible depreciation on machinery (A) + (B)</b>		<b><u>1,50,000</u></b>
<b>Depreciation allowable under section 32</b>		<b>1,86,000</b>

12. **Computation of interest payable under section 234B by Mr. Sachal**

Particulars	₹
Tax on total income of ₹ 10,80,000 [Business income of ₹ 8,10,000 + Income from other sources of ₹ 2,70,000]	1,36,500
Add: Education cess and SHEC@3%	<u>4,095</u>
<b>Tax on total income</b>	<b>1,40,595</b>
Less: Tax deducted at source	<u>25,000</u>
<b>Assessed Tax</b>	<b><u>1,15,595</u></b>
90% of assessed tax	1,04,036
Advance tax paid	1,03,000
Interest under section 234B is leviable since advance tax of ₹ 1,03,000 paid is less than ₹ 1,04,036, being 90% of assessed tax	
Number of months from 1 <sup>st</sup> April, 2018 to 11 <sup>th</sup> December, 2018, being the date of processing of return	9

Interest under section 234B@1% per month or part of a month for 9 months on ₹ 12,500 [i.e., difference between assessed tax of ₹ 1,15,595 and advance tax of ₹ 1,03,000 paid, being ₹ 12,595 which is rounded off to ₹ 12,500 under Rule 119A of Income-tax Rules, 1962]	1,125
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**Consequences for delay in filing return of income on or before the due date**

Interest under section 234A and fee under section 234F would be attracted for filing return of income beyond the due date specified under section 139(1).

**Interest under section 234A**

Since Mr. Sachal's accounts are audited under section 44AB, the due date for filing of return for A.Y. 2018-19, in his case, is 30.09.2018. Mr. Sachal has filed his return on 11.12.2018 i.e., interest under section 234A will be payable for 3 months (from 1.10.2018 to 11.12.2018) @ 1% per month or part of month on the amount of tax payable on the total income, as reduced by TDS and advance tax paid i.e., ₹ 12,595 rounded off to ₹ 12,500 under Rule 119A of Income-tax Rules, 1962

Interest u/s 234A = ₹ 12,500 x 1% x 3 = ₹ 375

**Fee for late filing of return under section 234F**

Since Mr. Sachal has furnished his return of income after the due date but before 31.12.2018 and his total income exceeds ₹ 5 lakhs, a fee of ₹ 5,000 will be payable by him.

13. Since Ms. Geetha has income only under the heads "Salaries", "Income from house property" and "Income from other sources", she does not fall under the category of a person whose accounts are required to be audited under the Income-tax Act, 1961. Therefore, the due date of filing return for A.Y.2018-19 under section 139(1), in her case, is 31<sup>st</sup> July, 2018. Since Ms. Geetha had submitted her return only on 29.9.2018, the said return is a belated return under section 139(4).

As per section 139(5), a return furnished under section 139(1) or a belated return u/s 139(4) can be revised, if she discovers any omission or wrong statement therein. Thus, a belated return under section 139(4) can also be revised. Therefore, Ms. Geetha can revise the return of income filed by her under section 139(4) in February 2019, to claim deduction under section 80D, since the time limit for filing a revised return is upto the end of the relevant assessment year, which is 31.03.2019.

However, she cannot revise return had she discovered this omission only on 02-04-2019, since it is beyond 31.03.2019, being the end of A.Y. 2018-19.

## SECTION B : INDIRECT TAXES

## QUESTIONS

- (1) All questions should be answered on the basis of the position of GST law as amended up to 31.10.2017.
- (2) The GST rates for goods and services mentioned in various questions are hypothetical and may not necessarily be the actual rates leviable on those goods and services. Further, GST compensation cess should be ignored in all the questions, wherever applicable.

1. Raman Ltd., a registered supplier in Mumbai (Maharashtra), has supplied goods to Sahil Traders and Jaggi Motors Ltd. located in Ahmedabad (Gujarat) and Pune (Maharashtra) respectively. Raman Ltd. has furnished the following details for the current month:

S. No.	Particulars	Sahil Traders (₹)	Jaggi Motors Ltd. (₹)
(i)	Price of the goods (excluding GST)	20,000	15,000
(ii)	Packing charges	600	
(iii)	Commission	400	
(iv)	Weighment charges		1,000
(v)	Discount for prompt payment (recorded in the invoice)		500

Items given in points (ii) to (v) have not been considered while arriving at price of the goods given in point (i) above.

Compute the GST liability [CGST & SGST or IGST, as the case may be] of Raman Ltd. for the given month. Assume the rates of taxes to be as under:

Particulars	Rate of tax
Central tax (CGST)	9%
State Tax (SGST)	9%
Integrated tax (IGST)	18%

Make suitable assumptions, wherever necessary.

**Note:** The supply made to Sahil Traders is an inter-State supply.

2. (i) Tirupati Traders, a registered supplier of goods, pays GST [CGST & SGST or IGST, as the case may be] under regular scheme. It has furnished the following particulars for a tax period:-

Particulars	₹
Value of intra-State supply of goods	12,000
Value of intra-State purchase of goods	10,000

**Note:**

- (i) Rates of CGST, SGST and IGST are 9%, 9% and 18% respectively.
- (ii) Both inward and outward supplies are exclusive of taxes, wherever applicable.
- (iii) All the conditions necessary for availing the input tax credit have been fulfilled.

Compute the net GST payable by Tirupati Traders during the given tax period assuming that there is no opening balance of input tax credit (ITC). Make suitable assumptions wherever required.

- (ii) Govind, a registered supplier, is engaged in providing services in the neighbouring States from his registered office located in Mumbai. He has furnished the following details in respect of the inward and outward supplies made during a tax period:-

Particulars	(₹)
Inter-State supply of services	1,80,000
Receipt of goods and services within the State	1,00,000

Assume the rates of taxes to be as under:-

Particulars	Rate
CGST	9%
SGST	9%
IGST	18%

**Note:**

- (i) Both inward and outward supplies are exclusive of taxes, wherever applicable.
- (ii) All the conditions necessary for availing the input tax credit have been fulfilled.

Compute the net GST payable by Govind during the given tax period. Make suitable assumptions if required.

3. Shipra Traders is a registered supplier of goods in Assam. It purchased goods valued at ₹ 10,000 from Kartik Suppliers located within the same State. Kartik Suppliers charged CGST & SGST separately in its invoice. Subsequently, Shipra Traders sold goods valuing ₹ 9,500 to Rabina Manufacturers located in Assam. 20% of the inputs purchased are still lying in stock and there was no opening stock of goods. Rate of CGST and SGST on supply and purchase of goods is 9% each. Calculate the net GST payable by Shipra Traders and input tax credit (ITC) to be carried forward, if any.

4. Granites Textiles Ltd. purchased a needle detecting machine on 8th July, 2017 from Makhija Engineering Works Ltd. for ₹ 10,00,000 (excluding GST) paying GST @ 18% on the same. It availed the ITC of the GST paid on the machine and started using it for manufacture of goods. The machine was sold on 22nd October, 2018 for ₹ 7,50,000 (excluding GST), as second hand machine to LT. Pvt. Ltd. The GST rate on supply of machine is 18%.

State the action which Granites Textiles Ltd. is required to take, if any, in accordance with the statutory GST provisions on the sale of the second-hand machine.

5. Royal Sweet Co., Delhi, a registered supplier, has furnished the details of the following few transactions which took place in November, 20XX:

S. No.	Date	Particulars	Date of invoice	Amount (₹)
(i)	11.11.20XX	Payment made to an advocate in Delhi	07.07.20XX	1,25,000
(ii)	20.11.20XX	Paid sitting fee to Director from Haryana for meeting held in Delhi on 15.10.20XX [Inter-State supply]	15.10.20XX	75,000

Assume the rates of taxes to be as under:-

Particulars	Rate
CGST	9%
SGST	9%
IGST	18%

You are required to compute GST [CGST & SGST/IGST, as the case may be] payable for the month of November, 20XX along with time of supply of the aforementioned activities.

6. Sahab Sales, an air-conditioner dealer in Janakpuri, Delhi, needs 4 air-conditioners for his newly constructed house in Safdarjung Enclave. Therefore, he transfers 4 air-conditioners [on which ITC has already been availed by it] from its stock, for the said purpose. Examine whether the said activity amounts to supply under section 7 of the CGST Act, 2017.

Further, a Janakpuri resident, Aakash, approached Sahab Sales. He sold an air-conditioner to Sahab Sales for ₹ 5,000. Aakash had bought the said air-conditioner six months before, for his residence. Does sale of the air conditioner by Aakash to Sahab Sales amount to supply under section 7 of the CGST Act, 2017?

7. Pure Oils, Delhi has started the supply of machine oils and high speed diesel in the month of April, 20XX. The following details have been furnished by it for the said month:-

Sl. No.	Particulars	₹*
(i)	Supply of machine oils in Delhi	2,00,000
(ii)	Supply of high speed diesel in Delhi	4,00,000
(iii)	Supply made through Fortis Lubricants - an agent of Pure Oils in Delhi	3,75,000
(iv)	Supply made by Pure Oils from its branch located in Punjab	1,80,000

\*excluding GST

Determine whether Pure Oils is liable for registration. Will your answer change, if Pure Oils supplies machine oils amounting to ₹ 2,50,000 from its branch located in Himachal Pradesh in addition to the above-mentioned supplies?

8. Royal Fashions, a registered supplier of designer outfits in Delhi, decides to exhibit its products in a Fashion Show being organised at Hotel Park Royal, Delhi on 4th January, 20XX. For the occasion, it gets the makeover of its models done by Aura Beauty Services Ltd., Ashok Vihar, for which a consideration is ₹ 5,00,000 (excluding GST) has been charged. Aura Beauty Services Ltd. issued a duly signed tax invoice on 10th February, 20XX showing the lumpsum amount of ₹ 5,90,000 inclusive of CGST and SGST @ 9% each. Royal Fashions made the payment the very next day. Answer the following questions:
- Examine whether the tax invoice has been issued within the time limit prescribed under law?
  - Tax consultant of Royal Fashions objected to the invoice raised suggesting that the amount of tax charged in respect of the taxable supply should be shown separately in the invoice raised by Aura Beauty Services Ltd. However, Aura Beauty Services Ltd. contended that there is no mandatory requirement of showing tax component separately in the invoice. You are required to examine the validity of the objection raised by tax consultant of Royal Fashions?

### SUGGESTED ANSWERS/HINTS

#### 1. Computation of GST liability

S. No.	Particulars	Sahil Traders (₹)	Jaggi Motors Ltd. (₹)
(i)	Price of goods	20,000	15,000
(ii)	Add: Packing charges (Note-1)	600	
(iii)	Add: Commission (Note-1)	400	
(iv)	Add: Weighment charges (Note-1)	-	1,000

(v)	Less: Discount for prompt payment (Note-2)	-	500
	Value of taxable supply	21,000	15,500
	<b>IGST payable @ 18% (Note-3)</b>	<b>3,780</b>	
	<b>CGST payable @ 9% (Note-4)</b>		<b>1,395</b>
	<b>SGST payable @ 9% (Note-4)</b>		<b>1,395</b>

**Notes:**

1. Incidental expenses, including commission and packing, charged by supplier to recipient of supply is includible in the value of supply. Weighment charges are also incidental expenses, hence includible in the value of supply [Section 15 of the CGST Act, 2017].
2. Since discount is known at the time of supply, it is deductible from the value in terms of section 15 of the CGST Act, 2017.
3. Since supply made to Sahil Traders is an inter-State supply, IGST is payable in terms of section 5 of the IGST Act, 2017.
4. Since supply made to Jaggi Motors Ltd. is an intra-State supply, CGST & SGST is payable on the same.

2. (i) **Computation of net GST payable**

Particulars	CGST (₹)	SGST (₹)
GST payable on intra-State supply of goods [Being an intra-State supply, CGST and SGST is payable on the same]	1,080 (₹12,000 × 9%)	1,080 (₹12,000 × 9%)
Less: Input tax credit (ITC) on intra-State purchase of goods [CGST and SGST paid on the intra-State purchases of goods]	900 (₹10,000 × 9%)	900 (₹10,000 × 9%)
Net GST payable	180	180

(ii) **Computation of net GST payable by Govind**

Particulars	₹
IGST @ 18% payable on inter-State supply of services [Being an inter-State supply, IGST is payable on the same in terms of section 5 of the IGST Act, 2017]	32,400 [1,80,000 × 18%]
Less: ITC of CGST @ 9% paid on intra-State receipt of goods and services	9,000

[Cross utilisation of CGST towards IGST]	[1,00,000 × 9%]
Less: ITC of SGST @ 9% paid on intra-State receipt of goods and services	<u>9,000</u> [1,00,000 × 9%]
[Cross utilisation of SGST towards IGST]	
<b>Net GST payable in cash</b>	<b>14,400</b>

**Note:**

- CGST shall first be utilised towards payment of CGST and the amount remaining, if any, be utilised towards the payment of IGST [Section 49 of the CGST Act, 2017].
- SGST shall first be utilised towards payment of SGST and the amount remaining, if any, may be utilised towards the payment of IGST [Section 49 of the CGST Act, 2017].

3. **Computation of net GST payable by Shipra Traders**

Particulars	CGST @ 9% (₹)	SGST @ 9% (₹)
GST payable on intra-State supply of goods [Being an intra-State supply, CGST and CGST is payable on the same]	855 [9,500 × 9%]	855 [9,500 × 9%]
Less: ITC on intra-State purchase of goods [ITC of CGST and SGST paid on intra-State purchase is available in full, even if some inputs are lying in stock]	<u>900</u> [10,000 × 9%]	<u>900</u> [10,000 × 9%]
<b>Net GST payable</b>	<b>Nil</b>	<b>Nil</b>
<b>Input tax credit carried forward in Electronic Credit Ledger</b>	<b>45</b>	<b>45</b>

- Section 18 of the CGST Act, 2017 read with the CGST Rules, 2017 provides that if capital goods or plant and machinery on which input tax credit has been taken are supplied outward by the registered person, he must pay an amount that is the higher of the following:
  - input tax credit taken on such goods reduced by 5% per quarter of a year or part thereof from the date of issue of invoice for such goods (i.e., input tax credit pertaining to remaining useful life of the capital goods), or
  - tax on transaction value.

Accordingly, the amount payable on supply of needle detecting machine shall be computed as follows:



Particulars	₹	₹
Input tax credit taken on the machine (₹ 10,00,000 × 18%)		1,80,000
Less: Input tax credit to be reversed @ 5% per quarter for the period of use of machine		
(i) For the year 2017-18 = (₹ 1,80,000 × 5%) × 3 quarters	27,000	
(ii) For the year 2018-19 = (₹ 1,80,000 × 5%) × 3 quarters	<u>27,000</u>	54,000
Amount required to be paid (A)		1,26,000
Duty leviable on transaction value (₹ 7,50,000 × 18%) (B)		1,35,000
Amount payable towards disposal of machine is higher of (A) and (B)		1,35,000

5. **Computation of GST payable for the month of November, 20XX**

S. No.	Particulars	Time of supply of services	CGST (₹)	SGST (₹)	IGST (₹)	Interest (₹)
(i)	Services from an advocate in Delhi	06.09.20XX [Note-1 & 3]	11,250	11,250	-	244 [Note-4]
(ii)	Director's Sitting fee	20.11.20XX [Note-2 & 3]	-	-	13,500	

**Notes:-**

- Services supplied by an individual advocate to any business entity located in the taxable territory is a notified service on which tax is payable on reverse charge basis by the recipient of services.
- Services supplied by a director of a company to the said company is a notified service on which tax is payable on reverse charge basis by the recipient of services.
- As per section 13 of the CGST Act, 2017, the time of supply of services in case of reverse charge is earliest of the following:-
  - Date of payment as entered in the books of account of the recipient or the date on which the payment is debited to his bank account, whichever is earlier, or
  - Date immediately following 60 days since the date of issue of invoice.

Provisions of time of supply as provided under section 13 of the CGST Act are also applicable for inter-State supply vide section 20 of the IGST Act.

In view of the aforesaid provisions, the time of supply and due date for payment of tax in the given cases would be determined as under:

- (i) Time of supply of the services is the date immediately following 60 days since the date of issue of invoice, i.e. 06.09.20XX. The due date for payment of tax is 20.10.20XX with return of September, 20XX.
  - (ii) Time of supply of service is 20.11.20XX and due date for payment of tax is 20.12.20XX with return of December, 20XX.
4. The due date for payment of tax in case (i) is 20.10.20XX with return of September, 20XX. However, the payment of tax is actually made on 11.11.20XX. Thus, payment of tax is delayed by 22 days.

In case of delayed payment of tax, interest @ 18% per annum is payable for the period for which the tax remains unpaid starting from the day succeeding the day on which such tax was due to be paid [Section 50 of the CGST Act, 2017 read with *Notification No. 13/2017 CT dated 28.06.2017*]. In view of the same, in the given case, interest payable would be as follows:

$$\text{Amount of interest payable} = ₹ 22,500 \times 18\% \times 22/365 = ₹ 244 \text{ (rounded off)}$$

6. Section 7 of the CGST Act, 2017 stipulates that in order to qualify as supply:
- (a) Supply should be of goods and/or services.
  - (b) Supply should be made for a consideration.
  - (c) Supply should be made in the course or furtherance of business.

Further, Schedule I of the CGST Act, 2017 illustrates the activities to be treated as supply even if made without consideration. One such activity is permanent transfer or disposal of business assets where input tax credit has been availed on such assets, i.e. said activity is to be treated as supply even if made without consideration. In view of said provisions, permanent transfer of air conditioners by Sahab Sales from its stock for personal use at its residence, though without consideration, would amount to supply.

However, sale of air-conditioner by Aakash to Sahab Sales will not qualify as supply under section 7 of the CGST Act, 2017 as although it is made for a consideration, but its not in the course or furtherance of business.

7. As per section 22 of the CGST Act, 2017, a supplier is liable to be registered in the State/Union territory from where he makes a taxable supply of goods or services or both, if his aggregate turnover in a financial year exceeds ₹ 20 lakh.

However, if such taxable supplies are made from any of the specified special category States, namely, States of Arunachal Pradesh, Assam, Manipur, Meghalaya, Mizoram, Nagaland, Sikkim, Tripura, Himachal Pradesh and Uttarakhand, he shall be liable to be registered if his aggregate turnover in a financial year exceeds ₹ 10 lakh.

As per section 2(6) of the CGST Act, 2017, aggregate turnover includes the aggregate value of:

- (i) all taxable supplies,

- (ii) all exempt supplies,
- (iii) exports of goods and/or services and
- (iv) all inter-State supplies of persons having the same PAN.

The above is computed on all India basis. Further, the aggregate turnover excludes central tax, State tax, Union territory tax, integrated tax and cess. Moreover, the value of inward supplies on which tax is payable under reverse charge is not taken into account for calculation of 'aggregate turnover'.

Further, the explanation to section 22 provides that the expression "aggregate turnover" shall include all supplies made by the taxable person, whether on his own account or made on behalf of **all his principals**.

Section 9 of the CGST Act, 2017 provides that CGST is not leviable on five petroleum products i.e. petroleum crude, motor spirit (petrol), high speed diesel, natural gas and aviation turbine fuel. As per section 2(47) of the CGST Act, 2017, exempt supply includes non-taxable supply. Thus, supply of high speed diesel in Delhi, being a non-taxable supply, is an exempt supply and is, therefore, includible while computing the aggregate turnover.

In the backdrop of the above-mentioned discussion, the aggregate turnover for the month of April, 20XX is computed as under:

S. No.	Particulars	Amount (in ₹)
(i)	Supply of machine oils in Delhi	2,00,000
(ii)	Add: Supply of high speed diesel in Delhi	4,00,000
(iii)	Add: Supply made through Fortis Lubricants - an agent of Pure Oils in Delhi	-
(iv)	Add: Supply made by Pure Oils from its branch located in Punjab	<u>1,80,000</u>
	Aggregate Turnover	7,80,000

Since the aggregate turnover does not exceed ₹ 20 lakh, Pure Oils is not liable to be registered.

If Pure Oils made supply of machine oils amounting to ₹ 2,50,000 from its branch in Himachal Pradesh in addition to the above supply, then threshold limit of registration will be reduced to ₹ 10 lakh as Himachal Pradesh is one of the specified Special Category States.

Aggregate Turnover in that case would be ₹ 7,80,000 + ₹ 2,50,000 = ₹ 10,30,000. So, if Pure Oils supplies machine oils amounting to ₹ 2,50,000 from its branch in Himachal Pradesh, then it is liable to be registered.

8. (i) As per section 31 of the CGST Act, 2017 read with the CGST Rules, 2017, in case of taxable supply of services, invoices should be issued before or after the provision of service, but within a period of 30 days [45 days in case of insurer/ banking company or financial institutions including NBFCs] from the date of supply of service.

In view of said provisions, in the present case, the tax invoice should have been issued in the prescribed time limit of 30 days from the date of supply of service i.e. upto 03.02.20XX. However, the invoice has been issued on 10.02.20XX.

In such a case, the time of supply as per section 13 of the CGST Act, 2017 would be 04.01.20XX i.e. earliest of the following:

- (a) Date of provision of service (04.01.20XX)
- (b) Date of receipt of payment (11.02.20XX)

- (ii) Section 31 of the CGST Act, 2017 read with the CGST Rules, 2017, *inter alia*, provides that tax invoice shall contain the following particulars-

- (a) Total value of supply of goods or services or both;
- (b) Rate of tax (central tax, State tax, integrated tax, Union territory tax or cess);
- (c) Amount of tax charged in respect of taxable goods or services (central tax, State tax, integrated tax, Union territory tax or cess);

The objection raised by the tax consultant of Royal Fashions suggesting that the amount of tax charged in respect of the taxable supply should be shown separately in the invoice raised by Aura Beauty Services Ltd., is valid in law. In the present case, the tax amount has not been shown separately in the invoice.

**Note:** GST law is in its nascent stage and has been subject to frequent changes. Although many clarifications have been issued in the last six months by way of FAQs or otherwise, many issues continue to arise on account of varying interpretations on several of its provisions. Therefore, alternate answers may be possible for the above questions depending upon the view taken.