PAPER – 1: ACCOUNTING

PART – I: ANNOUNCEMENTS STATING APPLICABILITY & NON-APPLICABILITY FOR NOVEMBER, 2014 EXAMINATION

A. Applicable for November, 2014 examination

Revision in the Criteria for classifying Level II Non-Corporate Entities

Due to recent changes in the enhancement of tax audit limit, the Council of the ICAI has recently decided to change the 1st criteria of Level II Non-Corporate Entities i.e. determination of SME on turnover basis from ₹ 40 lakhs to ₹ 1 Crore vide announcement "Revision in the Criteria for classifying Level II Non-Corporate Entities" issued by ICAI on 7th March, 2013. This revision is applicable with effect from the accounting year commencing *on or after April 1, 2012*.

B. Not applicable for November, 2014 examination

Ind ASs issued by the Ministry of Corporate Affairs

The MCA has hosted on its website 35 converged Indian Accounting Standards (Ind AS) without announcing the applicability date. These are the standards which are being converged by eliminating the differences of the Indian Accounting Standards vis-à-vis IFRS. These Ind ASs are not applicable for the students appearing in November, 2014 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 31st March, 2014:

	₹		₹
Inventory 1.4.2013	6,65,000	Bank Current Account	20,000
Discounts & Rebates	30,000	Cash in hand	8,000
Carriage Inwards	57,500	Debenture interest (for the period of 6 months ended 30.9.2013)	10,000
Patterns	3,75,000		
Rate, Taxes and Insurance	55,000	Interest (bank loan)	91,000
Furniture & Fixtures	1,50,000	Calls in Arrear @ ₹2 per share	10,000
Purchases	12,32,500	Equity share capital (2,00,000 shares of ₹ 10 each)	20,00,000

Wages	13,68,000	4% Debentures (repayable after 10 years)	5,00,000
Freehold Land	16,25,000	Bank Overdraft	7,57,000
Plant & Machinery	7,50,000	Trade Payables (for goods)	2,40,500
Engineering Tools	1,50,000	Sales	36,17,000
Trade Receivables	4,00,500	Rent (Cr.)	30,000
Advertisement	15,000	Transfer fees received	6,500
Commission & Brokerage	67,500	Profit & Loss A/c (Cr.)	67,000
Business Expenses	56,000	Repairs to Building	56,500
		Bad debts	25,500

The inventory (valued at cost or market value, which is lower) as on 31st March, 2014 was ₹ 7,08,000. 4% Debentures amounting ₹ 5,00,000 were issued on 1.04.2013. 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. Create debenture redemption reserve @ 10% of Debentures. Provide for income tax @ 30%. Corporate Divided Tax Rate @ 16.995%.

You are required to prepare Statement of Profit & Loss for the year ended 31st March, 2014 and Balance Sheet as on that date.

Cash Flow Statement

2. The summarized Balance Sheets of Z Ltd. as on 31st March, 2013 and 31st March, 2014 are as under:

Liabilities	2012-13	2013-14	Assets	2012-13	2013-14
	₹	₹		₹	₹
Equity share capital	15,00,000	20,00,000	Goodwill	5,75,000	4,50,000
12% Redeemable pref. share capital	7,50,000	5,00,000	Land & Building	10,00,000	8,50,000
General Reserve	2,00,000	3,50,000	Plant & Machinery	4,00,000	10,00,000
Profit & Loss A/c	1,50,000	2,40,000	Trade receivables	8,00,000	12,60,000
Trade Payables	2,75,000	4,15,000	Inventory	4,85,000	4,35,000
Outstanding	1,00,000	80,000	Cash and	1,25,000	90,000

Expenses			Bank		
Provision for Tax	2,00,000	2,50,000			
Proposed Dividend	2,10,000	2,50,000			-
	33,85,000	40,85,000		33,85,000	40,85,000

Additional Information:

(i) Depreciation charged on Plant & Machinery and Land & Building during the year was ₹ 50,000 and ₹ 1,00,000 respectively.

(ii) Income-tax ₹ 1,75,000 was paid during the year 2013-14.

Prepare Cash Flow Statement as per AS 3 (Revised), using indirect method.

Profit or Loss for Pre and Post Incorporation Period

3. The Business carried on by Kamal under the name "K" was taken over as a running business with effect from 1st April, 2013 by Sanjana Ltd., which was incorporated on 1st July, 2013. 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 31st March, 2014 were available.

	₹	₹
Sales: Company period	40,000	
Prior period	10,000	50,000
Selling Expenses	3,500	
Preliminary Expenses written off	1,200	
Salaries	3,600	
Directors' Fees	1,200	
Interest on Capital (Upto 30.6.2013)	700	
Depreciation	2,800	
Rent	4,800	
Purchases	25,000	
Carriage Inwards	1,019	43,819
Net Profit		6,181

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 31st March, 2014

Authorised capital:	₹
30,000 12% Preference shares of ₹ 10 each	3,00,000
3,00,000 Equity shares of ₹ 10 each	30,00,000
	33,00,000
Issued and Subscribed capital:	
24,000 12% Preference shares of ₹ 10 each fully paid	2,40,000
2,70,000 Equity shares of ₹ 10 each, ₹ 8 paid up	21,60,000
Reserves and surplus:	
General Reserve	3,60,000
Capital Reserve (profit realized on sale of plant)	1,20,000
Securities premium	75,000
Profit and Loss Account	6,00,000

On 1st April, 2014, the Company has made final call @ ₹ 2 each on 2,70,000 equity shares. The call money was received by 20th April, 2014. Thereafter, the company decided to capitalize its reserves by way of bonus at the rate of one share for every four shares held. Company decides to use Capital Reserve for bonus issue as it has been realized in cash.

Show necessary journal entries in the books of the company and prepare the extract of the balance sheet as on 30th April, 2014 after bonus issue.

Internal Reconstruction of a Company

5. Vinod Limited decided to reconstruct its business as it has accumulated huge losses. The following is the summarized Balance Sheet of the company as on 31.03.2014 before reconstruction:

Summarized Balance Sheet as on 31.03.2014

Particulars	₹	Particulars	₹
6,00,000 Equity shares of ₹ 10		Goodwill	10,40,000
each fully paid up	60,00,000	Patents	3,00,000
3,20,000, 6% Preference shares		Land & building	34,00,000
of ₹ 10 each fully paid up	32,00,000	Plant & machinery	4,00,000
6% Debentures (secured against		Investments (at cost)	4,40,000
land & building)	30,00,000	Trade receivables	34,80,000

Bank overdraft	11,60,000	Inventory	34,00,000
Trade payables	24,00,000	Profit & loss A/c	37,00,000
Provision for income tax	4,00,000		
	1,61,60,000		1,61,60,000

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

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

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

(3) Goodwill and Patent will be written off.

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

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

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

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

(8) There are pending contracts amounting to ₹ 20,00,000. These contracts are to be cancelled on payment of penalty @ 5% of pending contract amount.

(9) The income tax liability of the company is settled at ₹ 6,12,000. Provision for income tax will be raised accordingly.

(10) 1/3 of trade payables decided to forgo their claim.

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

You are required to pass the necessary Journal Entries.

Amalgamation of Companies

6. The following are the summarized Balance Sheets of P Ltd. and Q Ltd. as on 31st December, 2013:

Liabilities	P Ltd. ₹	Q Ltd. ₹	Assets	P Ltd. ₹	Q Ltd. ₹
Share Capital			Fixed Assets	7,00,000	2,50,000
Equity Shares of ₹ 10 each	6,00,000	3,00,000	Investment	80,000	80,000
10% Pref. Shares of ₹ 100 each	2,00,000	1,00,000	Current Assets: Inventory	– 2,40,000	3,20,000

Reserves and Surplus	3,00,000	2,00,000			
Secured Loans:			Trade receivables	4,20,000	2,10,000
12% Debentures	2,00,000	1,50,000	Cash at Bank	1,10,000	40,000
Current Liabilities:					
Trade payables	2,50,000	1,50,000			
	15,50,000	9,00,000		15,50,000	9,00,000

Details of Trade receivables and trade payables are as under:

	P Ltd. (₹)	Q Ltd. (₹)
Trade receivables		
Debtors	3,60,000	1,90,000
Bills Receivable	60,000	20,000
	4,20,000	2,10,000
Trade payables		
Sundry Creditors	2,20,000	1,25,000
Bills Payable	30,000	25,000
	2,50,000	1,50,000

Fixed Assets of both the companies are to be revalued at 15% above book value. Inventory in Trade and Debtors are taken over at 5% lesser than their book value. Both the companies are to pay 10% Equity dividend, Preference dividend having been already paid.

After the above transactions are given effect to, P Ltd. will absorb Q Ltd. on the following terms:

(i) 8 Equity Shares of ₹ 10 each will be issued by P Ltd. at par against 6 shares of Q Ltd.

(ii) 10% Preference Shareholders of Q Ltd. will be paid at 10% discount by issue of 10% Preference Shares of ₹ 100 each at par in P Ltd.

(iii) 12% Debentureholders of Q Ltd. are to be paid at 8% premium by 12% Debentures in P Ltd. issued at a discount of 10%.

(iv) ₹ 30,000 is to be paid by P Ltd. to Q Ltd. for Liquidation expenses. Sundry Creditors of Q Ltd. include ₹ 10,000 due to P Ltd.

Prepare:

(a) Journal entries in the books of P Ltd.

(b) Statement of consideration payable by P Ltd.

Average Due Date

7. A had the following bills receivable and bills payable against B. Calculate average due date when the payment can be made or received without any loss or gain of interest to either party.

Bills Receivable			Bills Payable		
Date of the Bill	Amount (₹)	Tenure in months	Date of bill	Amount (₹)	Tenure in months
1.6.13	18,000	3	29.5.13	12,000	2
5.6.13	15,000	3	3.6.13	18,000	3
9.6.13	20,000	1	10.6.13	20,000	2
12.6.13	16,000	2	13.6.13	14,000	2
20.6.13	24,000	3	27.6.13	22,000	1

Gazetted holiday intervening in the period are 15th August, 2013, 16th August, 2013, and 6th September, 2013.

Account Current

8. The following are the transactions that took place between Geet and Hari during the period from 1st October, 2013 to 31st March, 2014:

		₹
Oct.1, 2013	Balance due to Geet by Hari	6,000
Oct. 18, 2013	Goods sold by Geet to Hari	5,000
Nov. 16, 2013	Goods sold by Hari to Geet (due date November, 26)	8,000
Dec.7, 2013	Goods sold by Hari to Geet (due date December, 17)	7,000
Jan. 3, 2014	Promissory note given by Geet to Hari, at three months	10,000
Feb. 4, 2014	Cash paid by Geet to Hari	2,000
March 21, 2014	Goods sold by Geet to Hari	8,600
March 28, 2014	Goods sold by Hari to Geet (due date April, 8)	5,400

Draw up an Account Current upto March 31st, 2014 to be rendered by Geet to Hari, charging interest @10% per annum. Interest is to be calculated to the nearest rupee.

Self – Balancing Ledgers

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

	₹
Opening Balance of debtors ledger	40,000

Opening Balance of creditors ledger	20,000
Credit sales	92,000
Credit purchases	59,600
Transfer from Debtors' Ledger to Creditors' Ledger	2,200
Transfer from Creditors' Ledger to Debtors' Ledger	3,800
Bill receivable endorsed to Creditors	8,000
Endorsed Bills dishonoured	2,000
Bad Debts written off (after deducting bad debts recovered ₹ 600)	4,400
Provision for Doubtful Debts	1,100
Provision for Discount on Debtors	2,000
Reserve for Discount on Creditors	4,000
Cash Sales	6,000
Cash Purchases	8,000
Bill Receivable Collected on maturity	10,000
Bills Receivable discounted	12,000
Bills Payable matured	14,000
Discount allowed	3,000
Discount received	1,200
Allowances from Creditors	6,400
Discount allowed to debtors ₹ 1,000 was recorded as discount received from creditors	
Closing Debtors Balance (As per General Ledger Adjustment Account)	1,20,000(Cr.)
Closing Creditors Balance (As per General Ledger Adjustment Account)	60,000 (Dr)

Financial Statements of Not-For-Profit Organizations

10. From the following information, prepare Opening and Closing Balance Sheet of a Club:

	31st Dec. 2012	*31st Dec. 2013*
Building (subject to 10% depreciation for the current year)	60,000	?
Furniture (subject to 10% depreciation for the current year)	-	20,000
Stock of Sports Materials	5,000	2,000
Prepaid Insurance	3,000	6,000
Outstanding Subscription	12,000	8,000
Advance Subscription	6,000	4,000

Outstanding Locker Rent		6,000
Advance Locker Rent received	-	2,000
Outstanding Rent for Godown	6,000	3,000
12% General Fund Investments	2,00,000	2,00,000
Accrued Interest on above	-	4,000
Cash Balance	1,000	64,000
Bank Balance	2,000	-
Bank Overdraft		2,000

Entrance Fees received ₹ 20,000, Life Membership Fees received ₹ 20,000, surplus from income & expenditure Account ₹ 60,000. It is the policy of the club to treat 60% of entrance fees and 40% of Life Membership Fees as of revenue nature. The furniture was purchased on 01.01.2013

Accounts from Incomplete Records

11. Mr. H had ₹ 1,65,000 in the bank account on 1.1.2013 when he started his business. He closed his accounts on 31st March, 2014. His single entry books (in which he did not maintain any account for the bank) showed his position as follows:

	31.3.2013 ₹	*31.3.2014* ₹
Cash in hand	1,100	1,650
Stock in trade	10,450	15,950
Debtors	550	1,100
Creditors	2,750	1,650

On and from 1.2.2013, he began drawings ₹ 385 per month for his personal expenses from the cash box of the business. His account with the bank had the following entries:

	Deposits ₹	*Withdrawals* ₹
1.1.2013	1,65,000	-
1.1.2013 to 31.3.2013		1,22,650
1.4.2013 to 31.3.2014	1,26,500	1,48,500

The above withdrawals included payment by cheque of ₹ 1,10,000 and ₹ 33,000 respectively during the period from 1.1.2013 to 31.3.2013 and from 1.4.2013 to 31.3.2014 respectively for the purchase of machineries for the business. The deposits after 1.1.2013 consisted wholly of sale price received from the customers by cheques.

Draw up Mr. H's Statement of Affairs as at 31.3.2013 and 31.3.2014 respectively and work out his profit or loss for the year ended 31.3.2014.

Accounting for Hire -Purchase Transactions

12. (a) On 1.1.2011 Shaan Ltd. purchased a machine on hire purchase basis. The terms of agreement provided for 40% as cash down payment and the balance in three instalments of ₹ 1,63,000 on 31.12.2012, ₹ 1,20,000 on 31.12.2013 and ₹ 1,10,000 on 31.12.2014. The rate of interest charged by the vendor is 10% p.a. compound annually.

    You are required to calculate the cash Price and periodic interest charged by higher vendor.

    (b) On 1.1.2011 Beeta Ltd. purchased a machine from Yama Ltd. on hire purchase basis. The terms of agreement provided for 40% as cash down payment and the balance in three instalment of ₹ 1,30,000 on 31.12.2011, ₹ 1,42,000 on 31.12.2013 and ₹1,10,000 on 31.12.2014. The rate of interest charged by the vendor is 10% p.a. compounded annually. You are required to calculate the cash price when 2nd instalment is payable after two years.

Investment Accounts

13. Meera carried out the following transactions in the shares of Kumar Ltd.:

    (a) On 1st April, 2013 she purchased 40,000 equity shares of ₹ 1 each fully paid up for ₹ 60,000.

    (b) On 15th May 2013, Meera sold 8,000 shares for ₹ 15,200.

    (c) At a meeting on 15th June 2013, the company decided:

    (i) To make a bonus issue of one fully paid up share for every four shares held on 1st June 2013, and

    (ii) To give its members the right to apply for one share for every five shares held on 1st June 2013 at a price of ₹ 1.50 per share of which 75 paise is payable on or before 15th July 2013 and the balance, 75 paise per share, on or before 15th September, 2013.

    The shares issued under (i) and (ii) were not to rank for dividend for the year ending 31st December 2013.

    (a) Meera received his bonus shares and took up 4000 shares under the right issue, paying the sum thereon when due and selling the rights of the remaining shares at 40 paise per share; the proceeds were received on 30th September 2013.

    (b) On 15th March 2014, he received a dividend from Kumar Ltd. of 15 per cent in respect of the year ended 31st Dec 2013.

    (c) On 30th March he received ₹ 28,000 from the sale of 20,000 shares.

You are required to record these transactions in the Investment Account in Meera's books for the year ended 31st March 2014 transferring any profits or losses on these transactions to Profit and Loss account. Apply average cost basis.

Expenses and tax to be ignored.

Insurance Claim

14. The premises of Anmol Ltd. caught fire on 22nd January 2014, and the stock was damaged. The firm makes account up to 31st March each year. On 31st March, 2013 the stock at cost was ₹ 6,63,600 as against ₹ 4,81,100 on 31st March, 2012.

Purchases from 1st April, 2013 to the date of fire were ₹ 17,41,350 as against ₹ 22,62,500 for the full year 2012 -13 and the corresponding sales figures were ₹ 24,58,500 and ₹ 26,00,000 respectively. You are given the following further information:

(i) In July, 2013, goods costing ₹ 50,000 were given away for advertising purposes, no entries being made in the books.

(ii) During 2013-14, a clerk had misappropriated unrecorded cash sales. It is estimated that the defalcation averaged ₹ 1,000 per week from 1st April, 2013 until the clerk was dismissed on 18th August, 2013.

(iii) The rate of gross profit is constant.

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

Partnership Accounts

15. (a) R and G are partners sharing profits and losses in the ratio of 3:2 after allowing ₹ 1,000 p.m. salary for each partner. However, the accounts have not been prepared for the last three years. From the following details, you are required to calculate the distribution of profits between the partners in total for the three years.

	₹
Assets as at the end of 3rd year	1,60,000
Liabilities as at the end of 3rd year	40,000
Drawings for three years in addition to Salaries:	
R	30,000
G	22,000
Capital on commencement:	
R	50,000
G	40,000
Introduction of fresh capital during three years	
R	10,000

(b) T and W are equal partners in Timber Business. The Balance Sheet of their firm as on 31st March, 2014 was as under:

Liabilities	*Amount*	*Assets*	*Amount*
Capital Accounts		Fixed Assets	2,50,000
T	1,60,000	Stocks	65,200
W	1,60,000	Cash & Bank	54,800
Creditors & Other payables	50,000		
	3,70,000		3,70,000

On 1st April, 2014, P is admitted as an equal partner. Prior to his admission, the partners agreed to bring into the books of the firm, stocks worth ₹ 80,000 that was received free of cost from a Business Associate. Consequent to P's entry into the firm the capital base of the firm was expanded to ₹ 6 lakhs with all the partners agreeing to adopt the proportionate capital principle. P brought in the agreed sum of ₹ 2,80,000 (₹ 2,00,000 towards capital and ₹ 80,000 towards his share of goodwill). The partners decided not to raise goodwill in the books of accounts.

You are requested to show Capital Accounts of the three partners and the Balance Sheet of the Firm as on 1st April, 2014.

Accounting in Computerized Environment

16. (a) A large business entity wants to go in for an ERP (Enterprise Resource Planning) package. Which factors should it consider for the choice of an ERP package?

(b) Briefly describe the advantages and disadvantages of using an Enterprise Resource Planning (ERP) software in computerized accounting system.

AS 1 "Disclosure of Accounting Policies"

17. A limited has sold its building for ₹ 50 lakhs and the purchaser has paid the full price. The Company has given possession to the purchaser. The book value of the building is ₹ 35 lakhs. As at 31st March 2013, documentation and legal formalities are pending. The company has not recorded the sale. It has shown the amount received as advance. Do you agree with this treatment?

What accounting treatment should the buyer give in its financial statements?

AS 2 "Valuation of Inventories"

18. (a) A company had 5,000 units of stock "A", costing @ ₹ 50 each on 31.3.2014. Out of this stock, 3,000 units are to be supplied under a firm contract at ₹ 45 each. Show how the valuation will be done of such stock when

(i) the general selling price is ₹ 49 each.

(ii) the general selling price is ₹ 52 each.

AS 6 "Depreciation Accounting"

(b) An item of machinery was purchased on 1-4-2012 for ₹ 2,00,000. The WDV depreciation rate applicable to the machinery was 15%. The written down value of the machinery as on 31-3-2014 was ₹ 1,44,500. On 1-4-2014, the enterprise decided to change the method from written down value (WDV) to straight line method (SLM). The enterprise decided to write off the book value of ₹ 1,44,500, over the remaining useful life of machinery i.e. 5 years. Out of the total useful life 7 years, 2 years have already elapsed.

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

AS 7 "Construction Contracts

19. (a) PRZ & Sons Ltd. are Heavy Engineering contractors specializing in construction of dams. From the records of the company, the following data is available pertaining to year ended on 31st March, 2014. Using this data and applying the relevant Accounting Standard you are required to:

(i) Compute the amount of profit/loss for the year ended 31st March, 2014.

(ii) Arrive at the contract work in progress (cost incurred till date) as at the end of financial year 2013-14.

(iii) Determine the amount of revenue to be recognized out of the total contract value.

	(₹ crore)
Total Contract Price	2,400
Work Certified	1,250
Work pending certification	250
Estimated further cost to completion	1,750
Stage wise payments received	1,100
Progress payments in pipe line	300

AS-9 "Revenue Recognition"

(b) Victory Ltd. purchased goods on credit from Lucky Ltd. for ₹ 250 crores for export. The export order was cancelled. Victory Ltd. decided to sell the same goods in the local market with a price discount. Lucky Ltd. was requested to offer a price discount of 15%. The Chief Accountant of Lucky Ltd. wants to adjust the sales figure to the extent of the discount requested by Victory Ltd. Discuss whether this treatment is justified.

AS 10 "Accounting for Fixed assets"

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

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

AS 13 "Accounting for Investment"

(b) Albert Ltd. has made the following investments:

(i) Purchased the following equity shares from stock exchange on 1st June, 2013:

	Cost ₹
Scrip X	1,80,000
Scrip Y	50,000
Scrip Z	1,70,000
	4,00,000

(ii) Purchased government securities at a cost of ₹ 5,00,000 on 1st April, 2013.

How will you treat these investments as per applicable AS in the books of the company for the year ended on 31st March, 2014, if the values of these investments are as follows:

Shares	₹	₹
Scrip X	1,90,000	
Scrip Y	40,000	
Scrip Z	70,000	3,00,000
Government securities		7,00,000

SUGGESTED ANSWERS / HINTs

1. Kapil Ltd.

BALANCE SHEET
as at 31st March, 2014

		Particulars	Note No.	(₹)
I	Equity and Liabilities			
	(1)	Shareholders' Funds		
		(a) Share Capital	1	19,90,000
		(b) Reserves and Surplus	2	67,616
	(2)	Non-Current liabilities		
		(a) Long-term Borrowings [4% Debentures]		5,00,000
	(3)	Current Liabilities		
		(a) Trade Payables		2,40,500
		(b) Other Current Liabilities	3	8,28,000
		(c) Short-Term Provisions	4	3,99,384
		Total		40,25,500
II	ASSETS			
	(1)	Non-Current Assets		
		(a) Fixed Assets		
		(i) Tangible Assets	5	29,30,000
	(2)	Current Assets		
		(a) Inventories		7,08,000
		(b) Trade Receivables	6	3,59,500
		(c) Cash and Cash Equivalents	7	28,000
		Total		40,25,500

Kapil Ltd.

Statement of Profit and Loss for the year ended 31st March, 2014

	Particulars	Note No.	(₹)
I	Revenue from Operations		36,17,000
II	Other Income	8	36,500
III	Total Revenue [I + II]		36,53,500

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	4,40,000
	Total Expenses		32,53,500
V	Profit before Tax (III-IV)		4,00,000
VI	Tax Expenses @ 30%		(1,20,000)
VII	Profit for the period		2,80,000

Notes to Accounts:

1. Share Capital

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

2. Reserves and Surplus

Debenture Redemption Reserve		50,000
General Reserve		7000
Surplus i.e. Balance In Statement of Profit & Loss:		
Opening Balance	67,000	
Add: Profit for the period	2,80,000	
Less: Transfer to Reserve @ 2.5%	(7,000)	
Less: Proposed Equity Dividend [12% of (20,00,000-10,000)]	(2,38,800)	
Less: Corporate Dividend Tax [16.995% of 2,38,800]	(40,584)	
Less: Debenture Redemption Reserve [10% of ₹ 5,00,000]	(50,000)	10,616
		67,616

3. Other Current Liabilities

Bank Overdraft	7,57,000
Outstanding Expenses [25,000+36,000]	61,000
Interest accrued on Borrowings	10,000
	8,28,000

4. Short-term Provisions

Provision for Tax	1,20,000
Proposed Equity Dividend	2,38,800
Corporate Dividend Tax	40,584
	3,99,384

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	1,50,000	20%	30,000	1,20,000
	30,50,000		1,20,000	29,30,000

6. Trade Receivable

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

7. Cash & Cash Equivalent

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

8. Other Income

Miscellaneous Income (Transfer fees)	6,500
Rental Income	30,000
	36,500

9. Employee benefits expenses

Wages	13,68,000
Add: Outstanding wages	25,000
	13,93,000

10. Finance Cost

Interest on Bank loan	91,000
Debenture Interest	20,000
	1,11,000

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	25,000
	4,40,000

2. Cash Flow Statement for the year ending 31st March, 2014

		₹	₹
A.	Cash flow from operating activities		
	Profit and Loss A/c as on 31.3.2014		2,40,000
	Less: Profit and Loss A/c as on 31.3.2013		(1,50,000)
	Net profit for the year after taxation		90,000
	Add Transfer to General Reserve	1,50,000	
	Back: Provision for Tax	2,25,000	
	Proposed Dividend	2,50,000	6,25,000
	Profit before Tax		7,15,000
	Adjustment for Depreciation:		
	Land and Building	1,00,000	
	Plant and Machinery	50,000	1,50,000

	Goodwill written off		1,25,000
	Operating profit before working capital changes		9,90,000
	Adjustment for working capital changes:		
	Decrease in outstanding expenses	(20,000)	
	Decrease in inventory	50,000	
	Increase in trade receivables	(4,60,000)	
	Increase in trade payables	1,40,000	(2,90,000)
	Cash generated from operations		7,00,000
	Income tax paid		(1,75,000)
	Net Cash generated from operating activities (a)		5,25,000
B.	**Cash flow from investing activities**		
	Proceeds from sale of Building		50,000
	Purchase of Plant and Machinery		(6,50,000)
	Net Cash used in investing activities (b)		(6,00,000)
C.	**Cash flow from financing activities**		
	Proceeds from issuance of share capital		5,00,000
	Redemption of Preference Shares		(2,50,000)
	Dividend paid		(2,10,000)
	Net cash inflow from financing activities (c)		40,000
	Net increase in cash and cash equivalents during the year (a+b+c)		(35,000)
	Cash and cash equivalents at the beginning of the year		1,25,000
	Cash and cash equivalents at the end of the year		90,000

Working Notes:

1. Provision for Tax Account

	₹		₹
To Bank	1,75,000	By Balance b/d	2,00,000
To Balance c/d	2,50,000	By Profit and Loss A/c	2,25,000
	4,25,000		4,25,000

2. Plant and Machinery Account

	₹		₹
To Balance b/d	4,00,000	By Depreciation A/c	50,000
To Bank A/c (Purchases) (Balancing figure)	6,50,000	By Balance c/d	10,00,000
	10,50,000		10,50,000

3. Land and Building Account

	₹		₹
To Balance b/d	10,00,000	By Depreciation A/c	1,00,000
		By Bank a/c (Sales) (Balancing figure)	50,000
		By Balance c/d	8,50,000
	10,00,000		10,00,000

3 Statement showing the calculation of profits/losses for pre incorporation and Post incorporation period profits of Sanjana Ltd.

for the year ended 31st March, 2014

Particulars	Basis	Pre	Post
Sales (given)		10,000	40,000
Less: Purchases	1:3.3	5,814	19,186
Carriage Inwards	1:3.3	237	782
Gross Profit (i)		3,949	20,032
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	1,200	3,600
Total of Expenses(ii)		4,200	13,600
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

$\therefore$ Ratio is 3 : 9

But purchase price was 10% higher in the company period

$\therefore$ Ratio is 3 : 9 + 10%

3:9.9 = 1:3.3.

4. Journal Entries in the books of Manoj Ltd.

			₹	₹
1-4-2014	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….)			
20-4-2014	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 Reserve A/c	Dr.	1,20,000	
	General Reserve A/c	Dr.	3,60,000	
	Profit and Loss A/c	Dr.	1,20,000	
	To Bonus to shareholders A/c			6,75,000
	(For making provision for bonus issue of one share for every four shares held)			
	Bonus to shareholders A/c	Dr.	6,75,000	
	To Equity share capital A/c			6,75,000
	(For issue of bonus shares)			

Extract of Balance Sheet as at 30th April, 2014 (after bonus issue)

	₹
Authorised Capital	
30,000 12% Preference shares of ₹10 each	3,00,000
3,67,500 Equity shares of ₹10 each (refer W.N.)	36,75,000
Issued and subscribed capital	
24,000 12% Preference shares of ₹10 each, fully paid	2,40,000
3,37,500 Equity shares of ₹10 each, fully paid	33,75,000
(Out of the above, 67,500 equity shares @ ₹10 each were issued by way of bonus shares)	
Reserves and surplus	
Profit and Loss Account	4,80,000

Working Note:

The authorized capital should be increased as per details given below:	₹
Existing authorized Equity share capital	30,00,000
Add: Issue of bonus shares to equity shareholders (25% of ₹ 27,00,000)	6,75,000
	36,75,000

Note: It is assume that all legal formalities for increasing of authorized share capital have already been complied with before issue of bonus shares.

5. Journal Entries in the books of Vinod Limited

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

5.	Land & building A/c	Dr.	2,00,000	
	To Capital Reduction A/c			2,00,000
	(50% of balance land & building having book value ₹ 10,00,000, valued at ₹ 12,00,000, as per the reconstruction scheme)			
6.	Bank A/c	Dr.	4,00,000	
	Capital reduction A/c	Dr.	40,000	
	To Investment A/c			4,40,000
	(All the investment sold as per the reconstruction scheme)			
7.	Trade payables A/c	Dr.	8,00,000	
	To Capital reduction A/c			8,00,000
	(1/3 of Trade payables decided to forgo their claim as per the reconstruction scheme)			
8.	Capital reduction A/c	Dr.	64,20,000	
	To Goodwill A/c			10,40,000
	To Patents A/c			3,00,000
	To Provision for doubtful debts A/c			3,48,000
	To Inventory A/c			5,20,000
	To Bank A/c			1,00,000
	To Provision for tax A/c			2,12,000
	To Profit & loss A/c			37,00,000
	To Plant & machinery A/c (Bal. fig.)			2,00,000
	(Written off goodwill, patent, profit & loss, part value of stock, plant & machinery, penalty paid for cancellation of contracts and provision made for doubtful debts, income tax, as per the reconstruction scheme)			

6. (a) Journal Entries in the Books of P Ltd.

		Dr. ₹	*Cr.* ₹
Fixed Assets	Dr.	1,05,000	
To Revaluation Reserve			1,05,000
(Revaluation of fixed assets at 15% above book value)			
Reserve and Surplus	Dr.	60,000	

To Equity Dividend			60,000
(Declaration of equity dividend @ 10%)			
Equity Dividend	Dr.	60,000	
To Bank Account			60,000
(Payment of equity dividend)			
Business Purchase Account	Dr.	4,90,000	
To Liquidator of Q Ltd.			4,90,000
(Consideration payable for the business taken over from Q Ltd.)			
Fixed Assets (115% of ₹ 2,50,000)	Dr.	2,87,500	
Inventory (95% of ₹ 3,20,000)	Dr.	3,04,000	
Debtors	Dr.	1,90,000	
Bills Receivable	Dr.	20,000	
Investment	Dr.	80,000	
Cash at Bank	Dr.	10,000	
(₹ 40,000 – ₹ 30,000 dividend paid)			
To Provision for Bad Debts (5% of ₹ 1,90,000)			9,500
To Sundry Creditors			1,25,000
To 12% Debentures in Q Ltd.			1,62,000
To Bills Payable			25,000
To Business Purchase Account			4,90,000
To Capital Reserve (Balancing figure)			80,000
(Incorporation of various assets and liabilities taken over from Q Ltd. at agreed values and difference of net assets and purchase consideration being credited to capital reserve)			
Liquidator of Q Ltd.	Dr.	4,90,000	
To Equity Share Capital			4,00,000
To 10% Preference Share Capital			90,000
(Discharge of consideration for Q Ltd.'s business)			
12% Debentures in Q Ltd. (₹ 1,50,000 × 108%)	Dr.	1,62,000	
Discount on Issue of Debentures	Dr.	18,000	
To 12% Debentures			1,80,000
(Allotment of 12% Debentures to debenture holders of Q Ltd. at a discount of 10%)			
Sundry Creditors	Dr.	10,000	

To Sundry Debtors			10,000
(Cancellation of mutual owing)			
Capital Reserve	Dr.	30,000	
To Bank			30,000
(Being liquidation expenses reimbursed to Q Ltd.)			

(b) Statement of Consideration payable by P Ltd. for 30,000 shares (payment method)

Shares to be allotted $\frac{30,000}{6} \times 8$ = 40,000 shares of P Ltd.

Issued 40,000 shares of ₹ 10 each i.e	₹ 4,00,000	(i)
For 10% preference shares, to be paid at 10% discount		
₹ $\frac{1,00,000 \times 90}{100}$	₹ 90,000	(ii)
Consideration amount [(i) + (ii)]	₹ 4,90,000	

7. Calculation of Average Due Date (taking base date as 12th July, 2013)

Date	*Due date including days of grace*	*Amount (₹)*	*No. of Days from July 12, 2013*	*Products (₹)*	*Remarks*
1.6.13	4.9.13	18,000	54	9,72,000	Bills Receivable
5.6.13	8.9.13	15,000	58	8,70,000	
9.6.13	12.7.13	20,000	0		
12.6.13	14.8.13	16,000	33	5,28,000	
20.6.13	23.9.13	24,000	73	17,52,000	
		93,000		41,22,000	
29.5.13	1.8.13	12,000	20	2,40,000	Bills Payable
3.6.13	5.9.13	18,000	55	9,90,000	
10.6.13	13.8.13	20,000	32	6,40,000	
13.6.13	14.8.13	14,000	33	4,62,000	
27.6.13	30.7.13	22,000	18	3,96,000	
		86,000		27,28,000	

Difference of Products = ₹ 41,22,000 – ₹ 27,28,000 = ₹ 13,94,000

Difference of Amount = ₹ 93,000 – ₹ 86,000 = ₹ 7,000

Average Due Date $= \text{Base Date} + \dfrac{\text{Difference of Products}}{\text{Difference of Amount}}$

$= \text{July 12} + \dfrac{13,94,000}{7,000}$

= July 12 + 199.14 or 199 days

= 27th January, 2014

Note:

(i)	B/R of 12.6.13	Due date changed due to holidays i.e. immediately preceding working day
(ii)	B/P of 3.6.13	Due date changed due to holidays i.e. immediately preceding working day
(iii)	B/P of 13.6.13	Due date changed due to holidays i.e. immediately preceding working day

8. In the books of Geet

Hari in Account Current with Geet

(Interest upto 31st March, 2014 @ 10% p.a.)

Date	Due date	Particulars	No. of days till 31.3.14	Amount	Product	Date	Due date	Particulars	No. of days till 31.3.14	Amount	Product
2013	2013			₹		2013	2013			₹	
Oct. 1,	Oct. 1,	To Balance b/d	182	6,000	10,92,000	Nov. 16	Nov. 26	By Purchases	125	8,000	10,00,000
Oct. 18,	Oct. 18	To Sales	164	5,000	8,20,000	Dec 7	Dec. 17	By Purchases	104	7,000	7,28,000
2014	2014					2014	2014				
Jan. 3	Apr. 6	To Bills payable	(6)	10,000	(60,000)	Mar. 28	Apr. 8	By Purchases	(8)	5,400	(43,200)
Feb. 4	Feb. 4	To Cash	55	2,000	1,10,000	Mar. 31	Mar. 31	By Balance of product			3,63,200
Mar. 21	Mar. 21	To Sales	10	8,600	86,000			By Balance c/d		11,300	
Mar. 31	Mar. 31	To Interest (3,63,200 x 10%) /365		100	-						
				31,700	20,48,000					31,700	20,48,000

9. In Debtors Ledger

General Ledger Adjustment Account

Particulars	₹	Particulars	₹
To Debtors Ledger		By Balance b/d	40,000
Adjustment A/c:		By Debtors Ledger	
Discount Allowed (₹ 3,000+ ₹ 1,000)	4,000	Adjustment A/c:	
BadDebts(4,400+600)	5,000	Sales	92,000
Transfer to creditor ledger	2,200	Endorsed Bills	
Transfer from creditor ledger	3,800	receivable dishonoured	2,000
To Balance c/d (1,20,000 – 1,000)	1,19,000		
	1,34,000		1,34,000

In Creditors Ledger

General Ledger Adjustment Account

Particulars	₹	Particulars	₹
To Balance b/d	20,000	By Creditors Ledger Adjustment A/c	
To Creditors Leger		Transfer from Debtors' ledger	2,200
Adjustment A/c:		Transfer to Debtors' ledger	3,800
Purchases	59,600	Bill receivable endorsed to creditors	8,000
Endorsed Bills		Discount received	200
receivable dishonoured	2,000	(₹ 1,200– ₹1,000)	
		Allowances	6,400
		By Balance c/d (60,000+1,000)	61,000
	81,600		81,600

Notes:

(i) The following items do not appear in GLA Account in Debtors' ledger:

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

(ii) The following items do not appear in GLA Account in Creditors' ledger:

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

10. Balance Sheet as at 31st Dec., 2012

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

Balance Sheet as at 31st Dec. 2013

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

11. (a) Statement of Affairs as on 31st March, 2013

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

(b) Calculation of loss for 3 months (1.1.2013 to 31.3.2013)

	₹
Capital as on 31.3.2013	1,61,700
Add: Drawings for 2 months (1.2.2013 to 31.3.2013)	770
	1,62,470
Less: Capital as on 1.1.2013	(1,65,000)
Loss for 3 months	2,530

(c) Statement of Affairs as on 31st March, 2014

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

(d) Statement of Profit and Loss for the year ended 31.3.2014

Particulars	₹
Capital as on 31.3.2014	1,80,400
Add: Drawings (₹ 385 x 12)	4,620
	1,85,020
Less: capital as on 31.3.2013	(1,61,700)
Net profit for the year ended 31.3.14	23,320

Note: Depreciation has been ignored in the absence of information.

Working Notes:

	₹
1. **Bank balance as on 31.3.2013**	
Balance as on 1.1.2013	1,65,000
Less: Withdrawals during 1.1.2013 to 31.3.2013	(1,22,650)
Balance as on 31.3.2013	42,350
2. **Bank Balance as on 31.3.2014:**	
Balance as on 1.4.2013	42,350
Add: Deposits during the year	1,26,500
	1,68,850
Less: Withdrawals during the year	(1,48,500)
Bank Balance as on 31.3.2014	20,350

12. (a) Statement Showing the Computation of Cash Price and Periodic Interest

A *Instalment*	*B* *Balance due at the end after the payment of instalment*	*C* *Instalment Amount*	*D=B+C* *Total Amount Due at the end before the payment of instalment*	*E =* *Interest Dx10/110*	*F=D-E* *Balance Due at the Beginning*
III	NIL	1,10,000	1,10,000	10,000	1,00,000
II	1,00,000	1,20,000	2,20,000	20,000	2,00,000
I	2,00,000	1,63,000	3,63,000	33,000	3,30,000
	3,30,000	-	3,30,000	30,000	3,00,000

Let Cash Price be *X*

X = ₹ 3,00,000 + 40% of X

0.6 X = ₹ 3,00,000

X = ₹ 3,00,000/0.6 = ₹ 5,00,000, cash price = ₹ 5,00,000

(b) Statement Showing the Computation of Cash Price and Periodic Interest

A	B Balance Due at the end After the Payment of Instalment	C Instalment	D = B +C Total Amount Due at the end Before the payment of instalment	E =Dx10/110 interest	F=D-E Balance Due at the Beginning
III	Nil	1,10,000	1,10,000	10,000	1,00,000
II	1,00,000	1,42,000	2,42,000	22,000	2,20,000
	2,20,000	-	2,20,000	20,000	2,00,000
I	2,00,000	1,30,000	3,30,000	30,000	3,00,000

Let Cash Price be *X*

X = ₹ 3,00,000 + 40% of X

0.6 X = ₹ 3,00,000

X = ₹ 3,00,000/0.6 = ₹ 5,00,000, cash price = ₹ 5,00,000

13. In the books of Meera

Investment Account (Shares in Kumar Limited)

Date		*Particulars*	*No. of Shares*	*Income*	*Amount*	*Date*		*Particulars*	*No. of Shares*	*Income*	*Amount*
2013				₹	₹	*2013*				₹	₹
April 1	To	Bank (Purchases)	40,000	-	60,000	May 15	By	Bank (Sale)	8,000	-	15,200
May 15	To	Profit & Loss A/c (W.N.1)	-	-	3,200	Sept. 30	By	Bank (Sale of Right of 2,400 shares @ 40 paise per share)	-	-	960
June 15	To	Bonus Issue	8,000	-	Nil	2014					
July 15	To	Bank (@ 75 p. paid on 4,000 shares)	4,000	-	3,000	Mar. 15	By	Bank (Dividend @ 15% on ₹ 32,000)		4,800	-
Sept. 15	To	Bank (@ 75 p. paid on 4,000 shares)	-	-	3,000	Mar. 30	By	Bank (Sale)	20,000	-	28,000
2014 March 31	To	Profit & Loss A/c (W.N.2)			3,890	Mar. 31	By	Balance c/d $\left(\frac{24,000}{44,000}\times 53,040\right)$	24,000	-	28,930
	To	Profit & Loss A/c	-	4,800							
			52,000	4,800	73,090				52,000	4,800	73,090

Working Notes:

(1)	**Profit on Sale on 15-5-2013:**		
	Cost of 8,000 shares @ ₹1.50	₹ 12,000	
	Less: Sales price	₹ 15,200	
	Profit		₹ 3,200
(2)	**Cost of 20,000 shares sold:**		
	Cost of 44,000 shares (48,000 + 6,000)	₹ 54,000	
	Less: Amount received from rights	₹ 960	
	Cost of 44,000 shares		₹ 53,040
	$\therefore$ Cost of 20,000 shares $\left(\frac{₹\,53{,}040}{44{,}000 \text{ shares}} \times 20{,}000 \text{ shares}\right)$		₹ 24,110
	Profit on sale of 20,000 shares (₹ 28,000 – ₹ 24,110)		₹ 3,890

14. Ascertainment of rate of gross profit for the year 2012-13

Trading A/c for the year ended 31-3-2013

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

Rate of gross profit = $\frac{\text{GP}}{\text{Sales}} \times 100$

$$= \frac{5,20,000}{26,00,000} \times 100 = 20\%$$

Memorandum Trading A/c for the period from 1-4-2013 to 22-01-2014

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

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

Working Note:

Cash sales defalcated by the Accountant:

Defalcation period = 1.4.2013 to 18.8.2013 = 140 days

Since, 140 days / 7 weeks = 20 weeks

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

15. (a) Statement showing distribution of profits between the partners

	₹	₹
Assets at the end of the 3rd year		1,60,000
Less: Liabilities at the end of the 3rd year		(40,000)
		1,20,000
Add: Drawings including partnership salary:		
R[30,000 + (1,000 x 12 x 3)]	66,000	
G [22,000 + (1,000 x 12 x 3)]	58,000	1,24,000
		2,44,000
Less: Opening Capital:		
R	50,000	
G	40,000	(90,000)
		1,54,000
Less: Introduction of capital:		
R		(10,000)
Net Profit		1,44,000

Profit and Loss Appropriation Account for 3 years

Particulars	₹	Particulars	₹
To Partner's Salary		By Net Profit for three years	1,44,000
R (1,000 x 12 x 3)	36,000		
G (1,000 x 12 x 3)	36,000		
To Share of Profit			
R 43,200			
G 28,800	72,000		
	1,44,000		1,44,000

(b) Partners' Capital Accounts

Particulars	T	W	P	Particulars	T	W	P
	₹	₹	₹		₹	₹	₹
To T & W (Goodwill)	-	-	80,000	By Balance b/d	1,60,000	1,60,000	-
To Bank	40,000	40,000	-	By Bank	-	-	2,80,000
To Balance c/d	2,00,000	2,00,000	2,00,000	By P	40,000	40,000	-
				By Stock A/c	40,000	40,000	-
	2,40,000	2,40,000	2,80,000		2,40,000	2,40,000	2,80,000

Balance Sheet of M/s T, W & P as on 1st April, 20114

Liabilities	₹	*Assets*	₹
Capital Accounts		Fixed Assets	2,50,000
T	2,00,000	Stocks	1,45,200
W	2,00,000	Cash & Bank	2,54,800
P	2,00,000		
Creditors & Other Payables	50,000		
	6,50,000		6,50,000

16. (a) The business entity should consider the following factors while choosing an ERP package:

(i) Functional requirement of the organization: The ERP that matches most of the requirements of the organization should be preferred to others.

(ii) Reports available in the ERP: The organization should visualize the reporting requirements and choose a vendor which fulfils them.

(iii) Background of the vendors: The service and deliverable record of a vendor is extremely important in choosing the vendor.

(iv) Budget of the organization: The budget constraint and fund position of the enterprise should also be taken into consideration.

(b) The followings are the advantages of using an Enterprise Resource Planning (ERP) software in computerized accounting:

(i) It covers most of the common functions.

(ii) It generates most of the desired reports which are standardize across industries and acceptable to users.

(iii) It being an integrated package, duplication is avoided.

(iv) Much more information is made available by this package than what is available otherwise.

The followings are the disadvantages of ERP:

(i) The user may have to modify his business procedures to use ERP effectively.

(ii) It is often too expensive for small and medium sized organizations.

(iii) There may be implementation hurdles.

(iv) It is a complex software. Large number of modules, parameter settings and configuration makes it a complex.

17. Although legal title has not been transferred, the economic reality and substance is that the rights and beneficial interest in the immovable property have been transferred. Therefore, recording of acquisition/disposal (by the transferee and transferor respectively) would, in substance, represent the purchase/sale. In view of this A Ltd., should record the sales and recognize the profit of ₹15 lakhs in its profit and loss account. It should eliminate building from its balance sheet. In notes to accounts, it should disclose that building has been sold, full consideration has been received, possession has been handed over to the buyer and documentation and legal formalities are pending.

The buyer should recognize the building as an asset in his balance sheet and charge depreciation on it. The buyer should disclose in his notes to account that possession has been received however documentation and legal formalities are pending.

18. (a) (i) Valuation of stock as on 31.3.2014 when general selling price is ₹ 49 each.

Value 3,000 units at ₹ 45 each (lower of cost and net realizable value). Value remaining 2,000 units at ₹ 49 each (lower of cost and net realizable value).

Units	*Cost*	*NRV*	*Lower of cost and NRV*	*Valuation*
1	*2*	*3*	*4*	*5 = 1x4*
3000	50	45	45	1,35,000
2000	50	49	49	98,000
				2,33,000

Valuation of stock should be ₹ 2,33,000.

(ii) Valuation of stock as on 31.3.2014 when general selling price is ₹ 52 each

Units	*Cost*	*NRV*	*Lower of cost and NRV*	*Valuation*
1	*2*	*3*	*4*	*5 = 1x4*
3000	50	45	45	1,35,000
2000	50	52	50	1,00,000
				2,35,000

Valuation of stock should be ₹ 2,35,000.

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

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

	₹
Purchase price of plant as on 01-04-2012	2,00,000
Less: Depreciation as per SLM, for the year 2012-13 (₹ 2,00,000 ÷ 7 years)	28,571
Balance as on 31-3-2013	1,71,429
Less: Depreciation for the year 2013-14 (₹ 2,00,000 ÷ 7 years)	28,571
Balance as on 31-3-2014	1,42,858
Book value as per WDV method	1,44,500
Book value as per SLM	1,42,858
Deficiency	1,642

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

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

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

19. (a)

(i)	Calculation of profit/ loss for the year ended 31st March, 2014	(₹ in crores)
	Total estimated cost of construction (1,250 + 250 + 1,750)	3,250
	Less: Total contract price	(2,400)
	Total foreseeable loss to be recognized as expense	850

According to para 35 of AS 7 (Revised 2002) "Construction Contracts", when it is probable that total contract costs will exceed total contract revenue, the expected loss should be recognized as an expense immediately.

(ii)	Contract work-in-progress i.e. cost incurred to date	(₹ in crores)
	Work certified	1,250
	Work not certified	250
		1,500

(iii) Proportion of total contract value recognised as revenue

Percentage of completion of contract to total estimated cost of construction

= (1,500 / 3,250)×100 = 46.15%

Revenue to be recognized till date = 46.15% of ₹ 2,400 crores = ₹ 1,107.60 crores.

(b) Lucky Ltd. had sold goods to Victory Ltd on credit worth for ₹ 250 crores and the sale was completed in all respects. Victory Ltd's decision to sell the same in the domestic market at a discount does not affect the amount recorded as sales by Lucky Ltd. The price discount of 15% offered by Lucky Ltd. after request of Victory Ltd. was not in the nature of a discount given during the ordinary course of trade because otherwise the same would have been given at the time of sale itself. It is the special discount which is being allowed at the request of the buyer. Therefore, it would be appropriate to make a separate provision rather than to adjust the amount of revenue originally recorded. Therefore, such discount should be written off to the profit and loss account and not shown as deduction from the sales figure.

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

(b) As per para 14 and 15 of AS 13 'Accounting for Investments', current investments should be carried at lower of cost and fair value determined either on an individual investment basis or by category of investment, but not on an overall (or global) basis. Also as per para 17 of the standard, long-term investments are carried at cost except when there is a decline, other than temporary, in the value of a long term investment, the carrying amount is reduced to recognise the decline.

(i) If the investment in shares is intended to be held as current investment then scrip X should be valued at cost i.e. ₹1,80,000 (lower of cost and fair value), scrip Y should be valued at fair value i.e. ₹ 40,000 (lower of cost and fair value) and scrip Z should be valued at fair value i.e. ₹ 70,000 (lower of cost and fair value). The total loss of ₹ 1,00,000 (₹ 4,00,000 – ₹ 3,00,000) on scrip's purchased on 1st June, 2013 is to be charged to profit and loss account for the year ended 31st March, 2014.

If investment is intended to be held as long term investment then it will continue to be shown at cost in the balance sheet of the company. However, provision for diminution shall be made to recognize a decline, other than temporary, in the value of investments, such reduction being determined and made for each investment individually.

(ii) Value of government securities (purchased on 1st April, 2013) is to be shown at cost of ₹ 5,00,000 in the balance sheet as on 31.3.2014.

PAPER – 2: BUSINESS LAWS, ETHICS & COMMUNICATION

QUESTIONS

PART – A: BUSINESS LAWS

The Indian Contract Act, 1872

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

   (a) A entered into an agreement with S to deliver him 500 bags of sugar to be manufactured in his factory in a month. The sugar could not be manufactured because of strike by the workers and as a consequence, A failed to supply the agreed number of sugar bags to S. Decide whether A can be exempted from liability under the provisions of the Indian Contract Act, 1872.

   (b) M owes money to N under a contract. It is agreed between M, N and O that N shall henceforth accept O as his debtor instead of M. Referring to the provisions of the Indian Contract Act, 1872, state whether N can claim payment from O?

2. (a) Mr. Anand, is employed as a cashier on a monthly salary of ₹ 2,000 by ABC bank for a period of three years. X gave surety for Mr. Anand's good conduct. After nine months, the financial position of the bank deteriorates. Then Mr. Anand agrees to accept a lower salary of ₹ 1,500/- per month from Bank. Two months later, it was found that Mr. Anand has misappropriated cash since the time of his appointment. What is the liability of X?

   (b) B owes C a debt guaranteed by A. C does not sue B for a year after the debt has become payable. In the meantime, B becomes insolvent. Is A discharged? Decide with reference to the provisions of the Indian Contract Act, 1872.

The Negotiable Instruments Act, 1881

3. Discuss with reasons, in the following given conditions, whether X can be called as a 'holder' under the Negotiable Instruments Act, 1881:

   (i) X who obtains a cheque drawn by Y by way of gift.

   (ii) X, the payee of the cheque, who is prohibited by a court order from receiving the amount of the cheque.

   (iii) X, finds a cheque payable to bearer, on the road and retains it.

   (iv) X, the agent of Y, is entrusted with an instrument without endorsement by Y, who is the payee.

   (v) X, steals a blank cheque of A and forges A's signature.

4. A Bill is drawn and payable at particular adddress but does not contain drawee's name. Mr. Vinay who resides at the mentioned address accepts the bill. Is it a valid Bill?

The Payment of Bonus Act, 1965

5. An employee working in an establishment commits fraud during the accounting year 2009-2010, but continues to work during the subsequent accounting years 2010-2011 and 2011-2012, and has a clean record during the subsequent years. On the basis of the fraud committed in 2009-2010, the employee is dismissed from service at the end of the accounting year 2011-2012. In this case, does he lose the bonus for the accounting year of misconduct i.e. 2009-2010 or for all 3 accounting years ending with 2011-2012? Discuss in the light of the provisions of the Payment of Bonus Act, 1965.

6. A company employed 20 full–time and 5 part-time employees who were drawing salary of less than ₹ 10,000 per month. After completing service of 28 days, in an accounting year, 10 full-time employees submitted their resignations and left the service of the company. The Board of directors of this company decided not to give the bonus to the employees, who resigned, to the remaining full-time employees and to the part-time employees. Against the decision, all the employees applied to the authorities for relief.

   Decide, stating the provisions of the Payment of Bonus Act, 1965, whether the employees, who resigned, the remaining full-time employees and part-time employees will get relief.

The Employees' Provident Funds and Miscellaneous Provisions Act, 1952

7. State the provisions of the Employees' Provident Funds and Miscellaneous Provisions Act, 1952 regulating the quantum of contribution to be made by the employer and employee to the provident fund. Is it possible for an employee to increase the amount of his contribution to the provident fund more than the minimum contribution as statutorily prescribed?

8. A 60 years old district judge was appointed by the Central Government as Presiding Officer of the Employee's Provident Funds Appellate Tribunal for a period of 2 years. After one year, he resigns from his office and ceases to work with immediate effect without handing over the charge to his successor, who was not appointed by the Government till that date. Examine the validity of his action to cease work under the provisions of the Employees' Provident Funds and Miscellaneous Provisions Act, 1952.

The Payment of Gratuity Act, 1972

9. Mr. K, an employee in a coal mine with five days working in a week. K was not in continuous service during the financial year 2012-2013. He worked only for 150 days and due to arising of an accident during working in a mine, he was on leave with full pay for 45 days. Referring to the provisions of the Payment of Gratuity Act, 1972 decide, whether K is entitled to gratuity payable under the Act?

10. Bokaro steel plant decided to forfeit the amount of gratuity of its employees A, B and C on account of disorderly conduct and other acts which caused loss to the property belonging to the company. A, B and C committed the following acts:

(i) A refused to surrender the occupied land belonging to the company.

(ii) B committed theft under law involving offence of moral turpitude.

(iii) C after superannuation continued to occupy the quarter of the company for six months.

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

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

The Companies Act, 1956/ 2013

11. Explain the power of the company to close the register of members or debenture holders or other security holders as per the Companies Act, 2013. State the manner in which the corresponding provision given under the Companies Act, 1956 differs from the law given under new Act.

12. An allottee of shares in a Company brought action against a Director in respect of false statements in prospectus. The director contended that the statements were prepared by the promoters and he has relied on them. Is the Director liable under the circumstances? Decide referring to the provisions of the Companies Act, 2013.

13. A Company was incorporated on 6th July, 2014. The certificate of incorporation of the company was issued by the Registrar on 15th July, 2014. The company on 10th July, 2014 entered into a contract, which created its contractual liability. The company denies from the said liability on the ground that company is not bound by the contract entered into prior to issuing of certificate of incorporation. Decide, under the provisions of the Companies Act, 1956, whether the company can be exempted from the said contractual liability.

14. Write a note on the powers of the Central Government in regard to conversion of debentures and loans into shares of the company under the following heads:

    (i) When terms of issue of such debenture or terms of loan do not include term providing for an option of conversion;

    (ii) Matters considered in determining the terms and conditions of such conversion.

    (iii) Remedy available to the company if conversion or terms of conversion is not acceptable to it.

15. State the procedure for passing a resolution by Postal Ballot as per the Companies Act, 1956.

PART – B: ETHICS

16. Comment on the statement “Business is all green, only philosophy is grey”.

17. Explain "communications is another area in which ethical concern may arise".

18. What kind of pressure are faced by a finance and accounting professional working as an employee in an organization?

19. What are the common CSR policies ?

20. Explain the meaning of the terms 'ethics' and 'business ethics' and also state the requirements of 'business ethics'.

PART – C: COMMUNICATION

21. Explain clearly the process of Communication.

22. Explain the functions of interpersonal communication.

23. Explain the concept of "Negotiation". What are its techniques ?

24. Draft a letter informing the customer that his cheque has been dishonoured.

25. Draft the performa of affidavit for not having a Marriage certificate.

SUGGESTED ANSWERS/HINTS

1. (a) In this case Mr. A could not deliver the sugar bags as promised because of strike by the workers. This difficulty in performance cannot be considered as impossible of performance attracting Section 56 (Para 2) and hence A is liable to S for non-performance of contract.

   (b) Yes, a contract need not be performed when the parties to it agree to substitute a new contract for it or to rescind or alter it. (Section 62, Indian Contract Act, 1872). Here, in the given problem, novation has taken place as one of the parties has been replaced with a third party. Therefore, N can claim the money from O.

2. (a) If the creditor makes any variance (i.e. change in terms) without the consent of the surety, then surety is discharged as to the transactions subsequent to the change. In the instant case X is liable as a surety for the loss suffered by the bank due to misappropriation of cash by Anand during the first nine months but not for misappropriations committed after the reduction in salary. [Section 133, Indian Contract Act, 1872].

   (b) Discharge of surety: The problem is based on the provisions of section 137 of the Indian Contract Act, 1872 relating to discharge of surety. The section states that mere forbearance on the part of the creditor to sue the principal debtor and/or to enforce any other remedy against him would not, in the absence of any provision in the guarantee to the contrary, discharge the surety. In view of these provisions, A is not discharged from his liability as a surety.

3. **Person to be called as a holder**: As per section 8 of the Negotiable Instruments Act, 1881 'holder' of a Negotiable Instrument means any person entitled in his own name to the possession of it and to receive or recover the amount due thereon from the parties thereto.

   On applying the above provision in the given cases-

   (i) Yes, X can be termed as a holder because he has a right to possession and to receive the amount due in his own name.

   (ii) No, X is not a 'holder' because to be called as a 'holder' he must be entitled not only to the possession of the instrument but also to receive the amount mentioned therein.

   (iii) No, X is not a holder of the Instrument though he is in possession of the cheque, so is not entitled to the possession of it in his own name.

   (iv) No, X is not a holder. While the agent may receive payment of the amount mentioned in the cheque, yet he cannot be called the holder thereof because he has no right to sue on the instrument in his own name.

   (v) No, X is not a holder because he is in wrongful possession of the instrument.

4. Yes, it is a valid Bill and Mr. Vinay is liable thereon. The drawee may be named or otherwise indicated in the Bill with reasonable certainty. In the present case, the description of the place of residence indicates the name of the drawee and Mr. Vinay, by his acceptance, acknowledges that he is the person to whom the bill is directed (*Gray vs. Milner 1819*).

5. According to Section 9 of the Payment of Bonus Act, 1965, one of the grounds for disqualification for any bonus is fraud. An employee who is dismissed from service on the ground of misconduct as mentioned in section 9, is disqualified for any bonus and not merely for the bonus of the accounting year in which he is dismissed. Based on this provision, in the given case, the employee lose the bonus for all 3 three accounting years [*Pandian Roadways Corporation Ltd Vs Presiding officer(1996)2 CLR 1175(Mad)].*

6. In accordance with the provisions of Section 2(13) of the Payment of Bonus Act, 1965 any person other than an apprentice employed on a salary or wage not exceeding ₹ 10,000 per month in any industry to do any skilled or unskilled, manual, supervisory, managerial, administrative, technical or clerical work for hire or reward whether the terms of employment be express or implied is eligible for bonus. Further, in accordance with the provisions of Section 8 of the Payment of Bonus Act, 1965 every employee of an establishment covered under the Act is entitled to bonus from his employer in an accounting year provided he has worked in that establishment for not less than thirty working days in the year on a salary less than ₹ 10,000 per month.

   The problem as asked is based on the above provisions of the Act and the answer may be given as follows:

(a) As regards the employees who resigned : The employees who have resigned are not entitled to bonus because they have given their services only for 28 days in an accounting year although they are drawing salary less than ₹ 10,000 per mensem.

(b) As regards full time remaining employees: These employees are entitled to get the bonus as they fulfil both the requirements as stated under Sections 2 (13) and 8 of the Act. Although the employees in this case have been reduced to 10, once the Act is applicable, it continues to apply even if number of employees fall below 20.

(c) As regards part time employees: Even a part time employee is also entitled to bonus on the basis of total number of days worked by him in an accounting year. The Payment of Bonus Act, 1965 does not prohibit such employees as they fulfil all the requirements stated above [*Automobile Karmachari Sangh vs. Industrial Tribunal (1971)*].

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

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

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

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

8. Section 7 F of the Employees' Provident Funds and Miscellaneous Provisions Act, 1952 provides that the Presiding Officer of a Employees' Provident Funds Appellate Tribunal may by notice in writing under his hand addressed to the Central Government, resign his office provided that the Presiding Officer shall, unless he is permitted by the Central Government to relinquish his office sooner, continue to hold office until the expiry of three months from the date of receipt of such notice or until a person duly appointed as his successor enters upon his office or until the expiry of his term of office, whichever is the earliest.

   Hence, action of district judge is invalid as per above provisions. He should obtain permission from the Central Government to do so.

9. As per Section 2 A of the Payment of Gratuity Act, 1972 an employee shall be said to be in continuous service for a period if he has, for that period, been in uninterrupted service,

including service which may be interrupted on account of sickness, accident, leave, lay-off, strike or a lockout or cessation of work not due to any fault of an employee.

Where any employee (not being an employee employed in a seasonal establishment) is not in continuous service for any period of one year he shall be deemed to be in continuous service under the employer for the said period of one year, if the employee during the period of twelve calendar months preceding the date with reference to which calculation is to be made, has actually worked under the employer for not less than (i) one hundred and ninety days, in the case of any employee employed below the ground in a mine or in an establishment which works for less than six days in a week, and (ii) two hundred and forty days, in any other case.

For the purposes of calculating the number of days on which an employee has actually worked under an employer shall include the days on which the person was absent due to temporary disablement caused by accident arising out and in the course of his employment.

Thus, as per the above provisions, K is entitled for gratuity because he was in continuous service (150+45 days) more than 190 days in 2012-2013 and was working in a mine with 5 days in a week(less than six days in a week).

10. Forfeiture of Gratuity: In accordance with the provisions of Section 4(6) of the Payment of Gratuity Act, 1972, if the services of any employee have been terminated for any act, willful omission, or negligence causing any damage or loss to or destruction of, property belonging to the employer, the gratuity shall be forfeited to the extent of the damage or loss so caused; and if the services of such an employee have been terminated for any act which constitutes an offence involving moral turpitude, provided that such offence is committed by him in the course of his employment, the gratuity payable to the employee may be wholly or partially forfeited.

The problem asked in the question is based on the above provisions and the provisions of Section 4(1) of the Payment of Gratuity Act, 1972. Accordingly, gratuity shall be paid to the employee when he completes five years of continuous service on his superannuation, or on his retirement or resignation, or on his death or disablement due to accident or disease. The condition of the completion of five years' continuous service is not essential in case of the termination of the employment of any employee due to death or disablement. Looking to the provisions of Section 4(1), it is clear that withholding of gratuity is not permissible under any circumstances, except under those circumstances covered by Section 4(6). In *K. C. Mathew vs. Plantation Corporation of Kerala Ltd. 2001 LLR (2) (Ker)*, it was held that withholding of gratuity is not permissible except under those circumstances enumerated in Section 4(6) and that the right to gratuity is a statutory right and none can be deprived of it except as provided by the law. Therefore, the contention of Bokaro steel plant is wrong, to that extent.

The correctness of the decision taken by Bokaro steel plant regarding forfeiture of the gratuity amount of its employees A, B and C may be tested in the light of Section 4(6) of the Payment of Gratuity Act,1972 as referred above.

(i) Accordingly, the refusal of an employee to surrender the occupied land belonging to the company is not sufficient ground to withhold gratuity under Section 4(6) of the Payment of Gratuity Act, 1972 *[Travancore Plywood Industries Ltd. vs. Regional Joint Labour Commissioner [1966] II LLJ 85 Ker]* Hence, A's gratuity cannot be withheld.

(ii) The offence of theft committed by B, under law involves moral turpitude and his gratuity stands wholly forfeited in view of Section 4(6) of the Act *[relevant case is Bharat Gold Mines Ltd vs. Regional Labour Commissioner, 1987, 70 FJR 11 (Karnataka)].*

(iii) If the employer has to be paid any amount regarding any type of charge by the employee and if he has not paid for the same during the course of his service, then the employer can adjust the amount from the gratuity of the employee. In the instant case, C after superannuation continued to occupy the quarter of the company for six months. Therefore the company is entitled to charge the rent from him and after adjusting other dues the remaining amount of gratuity may be paid *[relevant case is Wazir Chand vs. Union of India 2001, LLR172 (SC)].*

11. **Power to close register of members or debenture holders or other security holders-** Section 91 of the Companies Act, 2013 deals with the closing of the register of members. The provision lays down that -

(i) **Closing of register of members, debenture holders or other security holder by giving previous notice-** A company may close the register of members or the register of debenture-holders or the register of other security holders for any period or periods not exceeding in the aggregate forty-five days in each year, but not exceeding thirty days at any one time, subject to giving of previous notice of at least seven days or such lesser period as may be specified by Securities and Exchange Board for listed companies or the companies which intend to get their securities listed, in such manner as may be prescribed.

(ii) **If the register of members or of debenture-holders or of other security holders is closed without giving the notice or after giving shorter notice** than that so provided, or for a continuous or an aggregate period in excess of the limits specified above, the company and every officer of the company who is in default shall be liable to a penalty of 5,000/- for every day subject to a maximum of one lakh rupees during which the register is kept closed.

Point of comparison with respect to the Companies Act, 1956-

- This section of 2013 Act replaces section 154(Power to close register of members or debenture holders) of the 1956 Act.

- The new Act of 2013 introduces the closure of the Registers of other security holders in the provision.
- Listed companies or the companies which intend to get their securities listed(i.e., the unlisted companies) close the register of members/ register of debenture-holders / the register of other security holders by giving a previous notice of at least 7 days/ such lesser period as may be specified by Securities and Exchange Board. This law pertaining to listed companies is lacking in the 1956 Act.
- In case of default with respect to the closure of register of member / register of debenture-holders / the register of other security holders, there the company and every officer of the company who is in default shall be liable to a penalty of five thousand rupees for every day during which register is closed but not exceeding one lakh rupees. This limit of penalty is lacking in 1956 Act.

12. Yes, the Director shall be held liable. A director can escape liability for mis-statements in a prospectus only on the grounds specified under Section 34 and 35 of the Companies Act, 2013. Relying on statements prepared by promoters is not a ground included there under. Accordingly, no defence shall be available to the Director.

    A Director shall not be liable if he puts up the following defences:

    (i) Such statement or omission in the prospectus was immaterial, or

    (ii) Director had reasonable grounds to believe, and did up to the time of issue of the prospectus believe, that the statement was true or the inclusion or omission was necessary(Section 34, the Companies Act, 2013)

    (iii) Where a person having consented to become a director of the company, withdrew his consent before the issue of the prospectus, and that it was issued without his authority or consent; or where the prospectus was issued without the knowledge or consent of a person, and that on becoming aware of its issue, he forthwith gave a reasonable public notice that it was issued without his knowledge or consent.(Section 35, the Companies Act, 2013).

13. **Certificate of Incorporation and the binding effect:** Upon the registration of the documents as required under the Companies Act, 1956 for incorporation of a company, and on payment of the necessary fees, the Registrar of Companies issues a Certificate that the company is incorporated (Section 34, the Companies Act, 1956).

    Section 35 of the Companies Act, 1956, provides that a certificate of incorporation issued by the Registrar is conclusive as to all administrative acts relating to the incorporation and as to the date of incorporation. The facts as given in the problem are similar to those in case of *Jubilee Cotton Mills v. Lewis (1924) A.C. 1958* where it was held that an allotment of shares made on the date after incorporation could not be declared void on the ground that it was made before the company was incorporated when the certificate of incorporation was issued at a later date.

Applying the above principles the contention of the company in this case cannot be tenable. It is immaterial that the certificate of incorporation was issued at a later date. Since the company came into existence on the date of incorporation stated on the certificate, it is quite legal for the company to enter into contracts. To conclude the contracts entered into by the company before the issue of certificate of incorporation shall be binding upon the company. The date of issue of certificate is immaterial.

14. (i) Under Section 81 of the Companies Act, 1956 where any debentures have been issued to or loans have been obtained from the Government by a company, whether such debentures have been issued or loans have obtained before or after the commencement of Companies Amendment Act, 1963 (w.e.f. 1.1.1964), the Central Government may, if in its opinion it is necessary in the public interest so to do, by order direct that such debentures or loans or any part thereof shall be converted into shares in the company on such terms and conditions as appear to that Government to be reasonable in the circumstances of the case, even if the terms of issue of such debentures or the terms of such loans do not include term providing for an option for such conversion.

(ii) In determining the terms and conditions of such conversion, the Central Government shall have due regard to the following circumstances:

(i) The financial position of the company;

(ii) The terms of issue of the debentures or the terms of the loans, as the case may be;

(iii) The rate of interest payable on the debentures or the loans;

(iv) The capital of the company, its loan liability, its reserves, its profits during the preceding five years; and

(v) The current market price of the shares in the company.

A copy of every order proposed to be issued by the Central Government shall be laid in draft before each House of Parliament.

(iii) Remedies open to the company: If the terms and conditions of such conversion are not acceptable to the company, the company may, within 30 days from the date of communication of such order or within such further time as may be granted by the Court, prefer an appeal to the court in regard to such terms and conditions and the decision of the Court on such appeal and, subject only to such decision, the order of the Central Government shall be final and conclusive.

15. A listed public company and in case of resolutions relating to such business as the Central Government may, by notification, declare to be conducted only by postal ballot, shall get any resolution passed by means of a postal ballot, instead of transacting the business in general meeting of the company. The term 'Postal Ballot' includes voting by electronic mode.

The procedure laid down in Section 192A is as under:

(i) Notice to shareholders: Where a company decides to pass any resolution by resorting to postal ballot, it shall send a notice to all the shareholders, along with a draft resolution explaining the reasons therefore and requesting them to send their assent within a period of 30 days from the date of posting of the letter;

(ii) Notice shall be sent by registered post acknowledgement: The notice shall be sent by registered post acknowledgement due or by any other method as may be prescribed by the Central Government in this behalf, and shall be annexed with the notice a postage pre-paid envelope for facilitating the communication of the assent or dissent of the shareholder to the resolution within the said period;

(iii) Appointment of scrutinizer: The board of directors shall appoint one scrutinizer, who is not in employment of the company, may be a retired judge or any person of repute, who, in the opinion of the board can conduct the postal ballot voting process in a fair and transparent manner;

(iv) Submission of report by the scrutinizer: The scrutinizer will be in position for 35 days (excluding holidays) from the date of issue of notice for annual general meeting. He is required to submit his final report on or before the said period.

(v) Resolution assented by majority: If a resolution is assented to by a requisite majority of the shareholders by means of postal ballot, it shall be deemed to have been passed at a general meeting convened in that behalf.

For this purpose the scrutinizer willing to be appointed is available at the registered office of the company for ascertaining the requisite majority.

(vi) Fraudulent defence or destroy of postal ballot: If a shareholder sends his assent or dissent in writing on a postal ballot and thereafter any person fraudulently defences or destroys the ballot paper or declaration of the identity of shareholder, such person shall be punishable with imprisonment for a term which may extend to six months or with fine or both;

(vii) Maintenance of register by scrutinizer: The scrutinizer shall maintain a register to record the consent received, including electronic media, mentioning the particulars of name, address, folio number, number of shares, nominal value of shares, whether the shares have voting, differential voting or non-rights and the scrutinizer shall also maintain record for postal ballot which are received in defaced or mutilated form. The postal ballot and all other papers relating to postal ballot will be under the safe custody of the scrutinizer till the Chairman considers, approves and signs the minutes of the meeting. Thereafter, the scrutinizer shall return the ballot papers and other related papers/register to the company so as to preserve such ballot papers and other related papers/registers safely till the resolution is given effect to.

16. The statement was given by the karl marx commenting on the business objectives said "*Business is all green, only philosophy is grey.*" By this line he meant that business is all

about profits and comfort for its rich owners and discomforts for all other sections of the society who are at the receiving end of the business. Despite such socialist ideology been relegated to the background due to fact that capitalism is being gradually accepted; business is still painted as essentially exploitative in nature. But one has to accept that much of the progress in the world would not have been possible without entrepreneurship and business which involves risk.

17. Communications is another area in which ethical concerns may arise. False and misleading advertising, as well as deceptive personal-selling tactics, anger consumers and can lead to the failure of a business. Truthfulness about product safety and quality are also important to consumers. The Food and Drug Regulatory Authorities need to ensure that customers are told the truth about product safety, quality, and effectiveness claims. Some manufacturers fail to provide enough information to consumers about differences or similarities between products. For *example*, a lawsuit filed by consumers against Johnson claimed that the company's Acuvue and 1-Day Acuvue contact lenses were actually the same product. Consumers were directed by the company to dispose of the 1-Day Acuvue lenses after one day's use. The suit claims that because the two products were identical, the lenses could have been worn up to two weeks. It is estimated that six million people who used contact lenses spent $1.1 billion on unnecessary replacements because of the company's misleading advertising. Johnson & Johnson agreed to pay up to $860 million to settle the complaints. Another important aspect of communications that may raise ethical concerns relates to product labelling. It is mandatory for cigarette manufacturers to indicate clearly on cigarette packing that smoking cigarettes is harmful to the smoker's health.

18. A finance and accounting professional may be under pressure to act or behave in ways that could directly or indirectly threaten compliance with the fundamental principles. Such pressure may be explicit or implicit; it may come from a supervisor, manager, director or another individual within the employing organization. A finance and accounting professional may face pressure to:

    - Act contrary to law or regulation.
    - Act contrary to technical or professional standards.
    - Facilitate unethical or illegal earnings management strategies.
    - Lie to, or otherwise intentionally mislead (including misleading by remaining silent) others, in particular:
    - The auditors of the employing organization; or
    - Regulators.
    - Issue, or otherwise be associated with, a financial or non-financial report that materially misrepresents the facts, including statements in connection with, for *example:*

The financial statements; Tax compliance; Legal compliance; or Reports required by securities regulators.

19. CSR Policies: Corporate Social Responsibility (CSR) refers to operating a business in a manner that accounts for the social and environmental impact created by the business. CSR means a commitment to developing policies that integrate responsible practices into daily business operations, and to reporting on progress made toward implementing these practices.

    Common CSR policies include:

    - Adoption of internal controls reform in the wake of Enron and other accounting scandals;
    - Commitment to diversity in hiring employees and barring discrimination;
    - Management teams that view employees as assets rather than costs;
    - High performance workplaces that integrate the views of line employees into decision-making processes;
    - Adoption of operating policies that exceed compliance with social and environmental laws;
    - Advanced resource productivity, focused on the use of natural resources in a more productive, efficient and profitable fashion (such as recycled content and product recycling); and
    - Taking responsibility for conditions under which goods are produced directly or by contract employees domestically or abroad.

20. Ethics: The term 'Ethics' has a variety of meanings. One of the meanings is 'Ethics' are the principles of conduct governing an individual or a group. Another definition describes ethics as relating to what is good or bad and having to do with moral duty and obligation.

    Business Ethics: In a broad sense, ethics in business refers to the application of day-to-day moral and ethical norms to business. Business ethics are the principles and standards that determine acceptable conduct in business organisation.

    Requirements: Being ethical in business requires acting with an awareness of -

    (a) The need for complying with rules (e.g) (i) laws of the land, (ii) customs and expectation of the community (iii) principles of morality (iv) policies of the organization and (v) general concerns such as the needs of others and fairness.

    (b) How the products, services and actions of a business enterprise, can affect its stakeholders (i.e. employees, customers, suppliers, shareholders and community society as a whole) either positively or negatively.

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

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

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

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

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

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

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

    - Inclusion is the need to establish identity with others.
    - Control is the need to exercise leadership and prove one's abilities.

- Affection is the need to develop relationships with people. Groups are an excellent way to make friends and establish relationships.

23. Negotiation: Negotiation occurs when two or more parties either individuals or groups discuss specific proposals in order to find a mutually acceptable agreement. Whether it is with an employer, family member or business associate, we all negotiate for things each day like higher salary, letter service or solving a dispute with a co worker or family member Negotiation is a common way of settling conflicts in business. When handled skillfully, negotiation can improve the position of one or even both but when poorly handled; it can leave a problem still unsolved and perhaps worse than before.

    Techniques for Negotiation:

    (a) Spiraling agreements: Begin by reaching a minimums agreement even though it is not related to the objectives and build, hit by hit, on this first agreement.

    (b) Changing of position: Formulate the proposals in a different way, without changing the final result.

    (c) Gathering information: Ask for information from the other party to clarify their position

    (d) Making the cake bigger: Offer alternatives that may be agreeable to the other party, without changing the terms.

    (e) Commitments: Formalize agreements orally and in writing before ending the negotiation.

24.

-----------Bank Ltd

----------Branch,
New Delhi

To,

Date…………

Regarding: Dishonour of cheque no.-------drawn on ----------, dated--------

Dear Sir,

We inform you that your above cheque due to insufficient fund in your account was not clear and was received back by us. The cheque has been sent to you by registered post dated --------- at your residential address.

Sd/-

Manager of the Bank

25. Affidavit

I, ...S/o.............R/o..............................do hereby solemnly affirm and declare an oath as under:

“That the marriage between......(name of spouses with details) solemnized with the Hindu rituals on.......... at-------(Name of place) .That due to inadvertence, I did not register my marriage with the concerned department and not having marriage certificate.

Date:…………………..   Signature

Place:………………….   Deponent

PAPER – 3: COST ACCOUNTING AND FINANCIAL MANAGEMENT

PART I: COST ACCOUNTING

QUESTIONS

Material

1. Aditya Agro Ltd. produces edible oils of different varieties. The monthly demand pattern for the finished products are as follows:

Mustard oil	45,000 Litre
Soybean oil	15,000 Litre
Olive oil	3,000 Litre

To produce one litre of Mustard oil, Soybean oil and Olive oil, 5 kg. of mustards, 6 kg. of soybeans and 4.5 kg. of olives are required respectively. There is no opening and closing stock of materials.

Aditya Agro Ltd. can purchase the materials either from the farmers directly or from the wholesale market. The company can purchase any quantity of materials from the wholesale market but in case of purchase from the farmers, it has to purchase the minimum specified quantity of materials at a time. Following is the material-wise summary related with the purchase of materials:

	Wholesale Market	Farmers
Mustard:		
Minimum Quantity to be purchased	Any quantity	13,50,000 kg.
Purchase price per kg. (₹)	15.00	12.50
Central Sales Tax (CST)*	2%	---
Transportation cost per purchase (₹)	6,000	15,000
Sorting and piling cost per purchase (₹)	----	1,200
Loading cost per 50 kg. (₹)	10.00	5.00
Unloading cost per 50 kg. (₹)	2.00	2.00
Soybean:		
Minimum Quantity to be purchased	Any Quantity	2,70,000 kg.
Purchase price per kg. (₹)	11.00	9.00
Value Added Tax (VAT)**	4%	---
Transportation cost per purchase (₹)	9,000	12,000
Sorting and piling cost per purchase (₹)	---	800
Loading cost per 50 kg. (₹)	10.00	3.00
Unloading cost per 50 kg. (₹)	2.00	2.00

Olive:		
Minimum Quantity to be purchased	Any Quantity	1,62,000 kg.
Purchase price per kg. (₹)	36.00	28.00
Import duty***	---	10%
Transportation Cost per purchase (₹)	3,000	11,000
Sorting and piling cost per purchase (₹)	1,800	---
Loading cost per 50 kg. (₹)	10.00	25.00
Unloading cost per 50 kg. (₹)	2.00	2.00

The company is paying 12.5% p.a. as interest to its bank for cash credit facility and ₹100 per 100 kg. as rent to the warehouse.

[*CST will be added with the purchase price of mustards; **VAT will not be added with the purchase price of soybeans; ***Import duty will be added with the purchase price of olives.]

You are required to

(i) Calculate the purchase cost of each material

(a) from Wholesale market

(b) from the Farmers

(ii) Calculate Economic Order Quantity of each material under the both options.

(iii) Recommend the best purchase option for the material 'olive'.

Labour

2. Jigyasa Boutiques LLP. (JBL) takes contract on job works basis. It works for various fashion houses and retail stores. It has employed 26 workers and pays them on time rate basis. On an average an employee is allowed 2 hours for boutique work on a piece of garment. In the month of March 2014, two workers Margaret and Jennifer were given 30 pieces and 42 pieces of garments respectively for boutique work. The following are the details of their work:

	Margaret	Jennifer
Work assigned	30 pcs.	42 pcs.
Time taken	28 hours	40 hours

Workers are paid bonus as per Halsey System. The existing rate of wages is ₹ 50 per hour. As per the new wages agreement the workers will be paid ₹ 55 per hour w.e.f. 1st April 2014. At the end of the month March 2014, the accountant of the company has calculated wages to these two workers taking ₹ 55 per hour.

(i) From the above information calculate the amount of loss that the company has incurred due to incorrect rate selection.

(ii) What would be the loss incurred by the JBL due to incorrect rate selection if it had followed Rowan scheme of bonus payment.

(iii) Amount that could have been saved if Rowan scheme of bonus payment was followed.

(iv) Do you think Rowan scheme of bonus payment is suitable for JBL?

Overheads

3. Vision Ltd. manufactures luggage trolleys for airports. The factory, in which the company undertakes all of its production, has two production departments- 'Fabrication' and 'Assembly', and two service departments- 'Stores' and 'Maintenance'.

The following information have been extracted from the company's budget for the financial year ended 31st March, 2014:

Allocated Overhead Costs	₹
Fabrication Department	15,52,000
Assembly Department	7,44,000
Stores Department	2,36,000
Maintenance Department	1,96,000
Other Overheads	₹
Factory rent	15,28,000
Factory building insurance	1,72,000
Plant & machinery insurance	1,96,000
Plant & Machinery Depreciation	2,65,000
Subsidy for staffs' canteen	4,48,000

Direct Costs	₹	₹
Fabrication Department:		
Material	63,26,000	
Labour	8,62,000	71,88,000
Assembly Department:		
Material	1,42,000	
Labour	13,06,000	14,48,000

The following additional information is also provided:

	Fabrication Department	Assembly Department	Stores Department	Maintenance Department
Floor area (square meters)	24,000	10,000	2,500	3,500
Value of plant & machinery (₹)	16,50,000	7,50,000	75,000	1,75,000
No. of stores requisitions	3,600	1,400	---	---
Maintenance hours required	2,800	2,300	400	---

No. of employees	120	80	38	12
Machine hours	30,00,000	60,000		
Labour hours	70,000	26,00,000		

Required:

(a) Prepare a table showing the distribution of overhead costs of the two service departments to the two production departments using step method; and

(b) Calculate the most appropriate overhead recovery rate for each department.

(c) Using the rates calculated in part (b) above, calculate the full production costs of the following job order:

Job number IGI2014

Direct Materials	₹ 1,15,200
Direct Labour:	
Fabrication Department	240 hours @ ₹ 18 per hour
Assembly Department	180 hours @ ₹ 18 per hour
Machine hours required:	
Fabrication Department	210 hours
Assembly Department	150 hours

Operating Costing

4. Gopal Milk Co-Operative Society (GMCS) collects raw milk from the farmers of Ramgarh, Pratapgarh and Devgarh panchayats and processes these milk to make various dairy products. GMCS has its own vehicles (tankers) to collect and bring the milk to the processing plant. Vehicles are parked in the GMCS's garage situated within the plant compound. Following are the some information related with the vehicles:

	Ramgarh	Pratapgarh	Devgarh
No. of vehicles assigned	4	3	5
No. of trips a day	3	2	2
One way distance from the processing plant	24 k.m.	34 k.m.	16 k.m.
Toll tax paid p.m. (₹)	2,850	3,020	---

All the 5 vehicles assigned to Devgarh panchayat, were purchased five years back at a cost of ₹ 9,25,000 each. The 4 vehicles assigned to Ramgarh panchayat, were purchased two years back at a cost of ₹ 11,02,000 each and the remaining vehicles assigned to Pratapgarh were purchased last year at a cost of ₹ 13,12,000 each. With the purchase of each vehicle a two years free servicing warranty is provided. A vehicle gives 10 kmpl mileage in the first two year of purchase, 8 kmpl in next two years and 6 kmpl afterwards. The vehicles are subject to depreciation of 10% p.a. on straight line basis irrespective of usage. A vehicle has the capacity to carry 25,000 litres of milk but on an average only 70% of the total capacity is utilized.

The following expenditure is related with the vehicles:

Salary to a Driver (a driver for each vehicle)	₹ 18,000 p.m.
Salary to a Cleaner (a cleaner for each vehicle)	₹ 11,000 p.m.
Allocated garage parking fee	₹ 1,350 per vehicle per month
Servicing cost	₹ 3,000 for every complete 5,000 k.m. run.
Price of diesel per litre	₹ 58.00

From the above information you are required to calculate

(i) Total operating cost per month for each vehicle. (Take 30 days for the month)

(ii) Vehicle operating cost per litre of milk.

Job Costing

5. Ares Plumbing and Fitting Ltd. (APFL) deals in plumbing materials and also provides plumbing services to its customers. On 12th August, 2014, APFL received a job order for a students' hostel to supply and fitting of plumbing materials. The work is to be done on the basis of specification provided by the hostel owner. Hostel will be inaugurated on 5th September, 2014 and the work is to be completed by 3rd September, 2014. Following are the details related with the job work:

Direct Materials

APFL uses weighted average method for the pricing of materials issues.

Opening stock of materials as on 12th August 2014:

- 15mm GI Pipe, 12 units of (15 feet size) @ ₹ 600 each
- 20mm GI Pipe, 10 units of (15 feet size) @ ₹ 660 each
- Other fitting materials, 60 units @ ₹ 26 each
- Stainless Steel Faucet, 6 units @ ₹ 204 each
- Valve, 8 units @ ₹ 404 each

Purchases:

On 16th August 2014:

- 20mm GI Pipe, 30 units of (15 feet size) @ ₹ 610 each
- 10 units of Valve @ ₹ 402 each

On 18th August 2014:

- Other fitting materials, 150 units @ ₹ 28 each
- Stainless Steel Faucet, 15 units @ ₹ 209 each

On 27th August 2014:

- 15mm GI Pipe, 35 units of (15 feet size) @ ₹ 628 each
- 20mm GI Pipe, 20 units of (15 feet size) @ ₹ 660 each
- Valve, 14 units @ ₹ 424 each

Issues for the hostel job:

On 12th August 2014:

- 20mm GI Pipe, 2 units of (15 feet size)
- Other fitting materials, 18 units

On 17th August 2014:

- 15mm GI Pipe, 8 units of (15 feet size)
- Other fitting materials, 30 units

On 28th August 2014:

- 20mm GI Pipe, 2 units of (15 feet size)
- 15mm GI Pipe, 10 units of (15 feet size)
- Other fitting materials, 34 units
- Valve, 6 units

On 30th August:

- Other fitting materials, 60 units
- Stainless Steel Faucet, 15 units

Direct Labour:

Plumber: 180 hours @ ₹ 50 per hour (includes 12 hours overtime)

Helper: 192 hours @ ₹35 per hour (includes 24 hours overtime)

Overtimes are paid at 1.5 times of the normal wage rate.

Overheads:

Overheads are applied @ ₹ 13 per labour hour.

Pricing policy:

It is company's policy to price all orders based on achieving a profit margin of 25% on sales price.

You are required to

(a) Calculate the total cost of the job.

(b) Calculate the price to be charged from the customer

Joint Products & By Products

6. Oleum Refinery Ltd. refines crude oil and produces two joint product Gasoline and HSD in the ratio of 4:6. The refining is done in three processes.

   Crude oil is first fed in Process-A, from where the two products Gasoline and HSD are get separated. After separation from Process-A, Gasoline and HSD are further processed in Process- B and Process- C respectively. During the month of July, 2014, 4,50,000 Ltr. of crude oil were processed in Process-A at a total cost of ₹ 1,71,99,775.

   In Process-B, Gasoline is further processed at a cost of ₹ 10,80,000.

   In Process- C, HSD is further processed at a cost of ₹ 1,35,000.

   The Input output ratio for the each process is as follows:

   Process- A 1 : 0.80

Process- B 1 : 0.95

Process- C 1 : 0.90

The details of sales during the month are:

	Gasoline	HSD
Quantity sold (Ltr.)	1,32,000	1,88,000
Sales price per Ltr.(₹)	68	46

There were no opening stocks. If these products were sold at split-off point, the selling price of Gasoline and HSD would be ₹ 64 and ₹ 41 per Ltr. respectively.

Required:

(i) Prepare a statement showing the apportionment of joint cost to Gasoline and HSD in proportion of sales value at split off point.

(ii) Prepare a statement showing the cost per Ltr. of each product indicating joint cost, processing cost and total cost separately.

(iii) Prepare a statement showing the product wise profit or loss for the month.

Standard Costing

7. The standard material cost for a normal mix of one tonne of product "Captain" based on:

Raw Material	Usage (in tonne)	Price per tonne
A	0.740	₹ 12,000
B	0.400	₹ 23,500
C	0.640	₹ 18,000

During the month of July, 2014, 18 tonnes of product "Captain" were produced from:

Raw Material	Consumption (tonnes)	Cost (₹)
A	13.12	1,62,000
B	7.10	1,65,200
C	11.50	2,07,000

Required to Calculate:

(i) Material Cost Variance

(ii) Material Price Variance

(iii) Material Usage Variance

(iv) Material Mix Variance

(v) Material Yield Variance

Marginal Costing

8. Maxim Ltd. manufactures a product "N-joy". In the month of August 2014, 14,000 units of the product "N-joy" were sold, the details are as under:

	(₹)
Sale Revenue	2,52,000
Direct Material	1,12,000
Direct Labour	49,000
Variable Overheads	35,000
Fixed Overheads	28,000

A forecast for the month of September 2014 has been carried out by the General manger of Maxim Ltd. As per the forecast, price of direct material and variable overhead will be increased by 10% and 5% respectively.

Required to calculate:

(i) Number of units to be sold to maintain the same quantum of profit that made in August 2014.

(ii) Margin of safety in the month of August 2014 and September 2014.

Budget and Budgetary Control

9. A Light Motor Vehicle manufacturer has prepared sales budget for the next few months, and the following draft figures are available:

Month	No. of vehicles
October	4,000
November	3,500
December	4,500
January	6,000
February	6,500

To manufacture a vehicle, a standard cost of ₹ 2,85,700 is incurred and sold through dealers at an uniform selling price of ₹ 3,95,600 to customers. Dealers are paid 12.5% commission on selling price on sale of a vehicle.

Apart from other materials four units of Part-X are required to manufacture a vehicle. It is a policy of the company to hold stocks of Part-X at the end of the each month to cover 40% of next month's production. 4,800 units of Part-X are in stock as on 1st October.

There are 950 nos. of completed vehicles are in stock as on 1st October and it is policy to have stocks at the end of each month to cover 20% of the next month's sales.

You are required to

(a) Prepare Production budget (in nos.) for the month of October, November, December and January.

(b) Prepare a Purchase budget for Part-X (in units) for the months of October, November and December.

(c) Calculate the budgeted gross profit for the quarter October to December.

Miscellaneous

10. (a) What is Cost accounting? Enumerate its important objectives.

(b) What are the reasons for disagreement of profits as per cost accounts and financial accounts? Discuss.

(c) What is cost plus contract? State its advantages.

(d) What is inter-process profit? State its advantages and disadvantages.

SUGGESTED HINTS/ANSWERS

1. (i) Calculation of Purchase Cost per Kg. of Materials

	Wholesale Market (₹)	Farmers (₹)
Mustard:		
Purchase price	15.00	12.50
Add: Central Sales Tax @ 2%	0.30	---
Add: Loading Cost	0.20 (₹ 10 ÷ 50 Kg.)	0.10 (₹ 5 ÷ 50 Kg.)
Add: Unloading Cost	0.04 (₹ 2 ÷ 50 Kg.)	0.04 (₹ 2 ÷ 50 Kg.)
	15.54	12.64
Soybean:		
Purchase price	11.00	9.00
Add: Loading Cost	0.20 (₹ 10 ÷ 50 Kg.)	0.06 (₹ 3 ÷ 50 Kg.)
Add: Unloading Cost	0.04 (₹ 2 ÷ 50 Kg.)	0.04 (₹ 2 ÷ 50 Kg.)
	11.24	9.10
Olive:		
Purchase price	36.00	28.00
Add: Import duty @ 10%	---	2.80
Add: Loading Cost	0.20 (₹ 10 ÷ 50 Kg.)	0.50 (₹ 25 ÷ 50 Kg.)

Add: Unloading Cost	0.04 (₹ 2 ÷ 50 Kg.)	0.04 (₹ 2 ÷ 50 Kg.)
	36.24	31.34

(ii) Economic Order Quantity (E.O.Q) = $\sqrt{\dfrac{2 \times \text{Annual requirement} \times \text{Ordering cost}}{\text{Carrying cost per kg. per annum}}}$

Annual Requirement (A) :

Commodity		Quantity (Kg.)
Mustard	(45,000 Ltr. × 5 Kg. × 12 months)	27,00,000
Soybean	(15,000 Ltr. × 6 Kg. × 12 months)	10,80,000
Olive	(3,000 Ltr. × 4.5 Kg. × 12 months)	1,62,000

Cost per Order (O):

	Wholesale Market (₹)	Farmers (₹)
Mustard:		
- Transportation cost	6,000	15,000
- Sorting and piling cost	---	1,200
	6,000	16,200
Soybean:		
- Transportation cost	9,000	12,000
- Sorting and piling cost	---	800
	9,000	12,800
Olive:		
- Transportation cost	3,000	11,000
- Sorting and piling cost	1,800	---
	4,800	11,000

Carrying Cost per Kg. per annum (C × i):

	Wholesale Market (₹)	Farmers (₹)
Mustard:		
- Interest on cash credit	1.9425 (₹ 15.54 × 12.5%)	1.5800 (₹ 12.64 × 12.5%)
- Warehouse rent*	1.0000	1.0000
	2.9425	2.5800

Soybean:		
- Interest on cash credit	1.4050 (₹ 11.24 × 12.5%)	1.1375 (₹ 9.10 × 12.5%)
- Warehouse rent	1.0000	1.0000
	2.4050	2.1375
Olive:		
- Interest on cash credit	4.5300 (₹ 36.24 × 12.5%)	3.9175 (₹ 31.34 × 12.5%)
- Warehouse rent	1.0000	1.0000
	5.5300	4.9175

* Warehouse rent per Kg. = $\frac{₹100}{100\text{Kg.}}$ = ₹ 1

Calculation of E.O.Q for each material under the both options

	Wholesale Market (Kg.)	Farmers (Kg.)
Mustard	$\sqrt{\frac{2\times 27,00,000\text{Kg.}\times ₹6,000}{₹2.9425}}$ = 1,04,933.53	$\sqrt{\frac{2\times 27,00,000\text{Kg.}\times ₹16,200}{₹2.5800}}$ = 1,84,138.47
Soybean	$\sqrt{\frac{2\times 10,80,000\text{Kg.}\times ₹9,000}{₹2.4050}}$ = 89,906.40	$\sqrt{\frac{2\times 10,80,000\text{Kg.}\times ₹12,800}{₹2.1375}}$ = 1,13,730.98
Olive	$\sqrt{\frac{2\times 1,62,000\text{Kg.}\times ₹4,800}{₹5.5300}}$ = 16,769.90	$\sqrt{\frac{2\times 1,62,000\text{Kg.}\times ₹11,000}{₹4.9175}}$ = 26,921.34

(iii) Selection of best purchase option for the purchase of Olives

	Wholesale Market	Farmers
Annual Requirement (A) (Kg.)	1,62,000	1,62,000
Order Quantity (Q)	16,769.90	1,62,000
No. of orders $\left(\frac{A}{Q}\right)$	9.66 or 10	1
Average Inventory $\left(\frac{Q}{2}\right)$ (Kg.)	8,384.95	81,000

Ordering Cost (₹)	(I)	48,000 (10 Orders × ₹ 4,800)	11,000 (1 Order × ₹ 11,000)
Carrying Cost (₹) (Average Inventory × Carrying cost per kg.)	(II)	46,368.77 (8,384.95 Kg. × ₹ 5.5300)	3,98,317.5 (81,000 Kg. × ₹ 4.9175)
Purchase Cost (₹)	(III)	58,70,880 (1,62,000 Kg. × ₹ 36.24)	50,77,080 (1,62,000 Kg. × ₹ 31.34)
Total Cost	(I) + (II) + (III)	59,65,248.77	54,86,397.50

Purchasing olives direct from the farmers is the best purchase option for the Aditya Agro Ltd.

2.

	Margaret	Jennifer
No. of garments assigned (Pieces.)	30	42
Hour allowed per piece (Hours)	2	2
Total hours allowed (Hours)	60	84
Hours Taken (Hours)	28	40
Hours Saved (Hours)	32	44

(i) Calculation of loss incurred due to incorrect rate selection.

(While calculating loss only excess rate per hour has been taken)

	Margaret (₹)	Jennifer (₹)	Total (₹)
Basic Wages	140 (28 Hrs. × ₹ 5)	200 (40 Hrs. × ₹ 5)	340
Bonus (as per Halsey Scheme) (50% of Time Saved × Excess Rate)	80 (50% of 32 Hrs. × ₹ 5)	110 (50% of 44 Hrs. × ₹ 5)	190
Excess Wages Paid	220	310	530

(ii) Amount of loss if Rowan scheme of bonus payment were followed

	Margaret (₹)	Jennifer (₹)	Total (₹)
Basic Wages	140.00 (28 Hrs. × ₹ 5)	200.00 (40 Hrs. × ₹ 5)	340.00

Bonus (as per Rowan Scheme) $\left(\frac{\text{Time Taken}}{\text{Time Allowed}} \times \text{Time Saved} \times \text{Excess Rate}\right)$	74.67 $\left(\frac{28}{60} \times 32 \times ₹5\right)$	104.76 $\left(\frac{40}{84} \times 44 \times ₹5\right)$	179.43
Excess Wages Paid	214.67	304.76	519.43

(iii) Calculation of amount that could have been saved if Rowan Scheme were followed

	Margaret (₹)	Jennifer (₹)	Total (₹)
Wages paid under Halsey Scheme	220.00	310.00	530.00
Wages paid under Rowan Scheme	214.67	304.76	519.43
Difference (Savings)	5.33	5.24	10.57

(iv) Rowan Scheme of incentive payment has the following benefits, which is suitable with the nature of business in which Jigyasa Boutique LLP operates:

(i) Under Rowan Scheme of bonus payment, workers cannot increase their earnings or bonus by merely increasing its work speed. Bonus under Rowan Scheme is maximum when the time taken by a worker on a job is half of the time allowed. As this fact is known to the workers, therefore, they work at such a speed which helps them to maintain the quality of output too.

(ii) If the rate setting department commits any mistake in setting standards for time to be taken to complete the works, the loss incurred will be relatively low.

3. (a) Table of Primary Distribution of Overheads

Particulars	Basis of Apportionment	Total Amount	Production Department		Service Departments	
			Fabrication	Assembly	Stores	Maintenance
Overheads Allocated	Allocation	27,28,000	15,52,000	7,44,000	2,36,000	1,96,000
Direct Costs	Actual	86,36,000	71,88,000	14,48,000	---	---
Other Overheads:						
Factory rent	Floor Area (48:20:5:7)	15,28,000	9,16,800	3,82,000	95,500	1,33,700
Factory building insurance	Floor Area (48:20:5:7)	1,72,000	1,03,200	43,000	10,750	15,050
Plant & Machinery insurance	Value of Plant & Machinery (66:30:3:7)	1,96,000	1,22,038	55,472	5,547	12,943
Plant & Machinery Depreciation	Value of Plant & Machinery (66:30:3:7)	2,65,000	1,65,000	75,000	7,500	17,500

Canteen Subsidy	No. of employees (60:40:19:6)	4,48,000	2,15,040	1,43,360	68,096	21,504
		1,39,73,000	1,02,62,078	28,90,832	4,23,393	3,96,697

Re-distribution of Service Departments' Expenses:

Particulars	Basis of Apportionment	Production Department		Service Departments	
		Fabrication	Assembly	Stores	Maintenance
Overheads as per Primary distribution	As per Primary distribution	1,02,62,078	28,90,832	4,23,393	3,96,697
Maintenance Department Cost	Maintenance Hours (28:23:4:-)	2,01,955	1,65,891	28,851	(3,96,697)
		1,04,64,033	30,56,723	4,52,244	---
Stores Department	No. of Stores Requisition (18:7:-:-)	3,25,616	1,26,628	(4,52,244)	
		1,07,89,649	31,83,351	---	---

(b) Overhead Recovery Rate

Department	Apportioned Overhead (₹) (I)	Basis of Overhead Recovery Rate (II)	Overhead Recovery Rate (₹) [(I) ÷ (II)]
Fabrication	1,07,89,649	30,00,000 Machine Hours	3.60 per Machine Hour
Assembly	31,83,351	26,00,000 Labour Hours	1.22 per Labour Hour

(c) Calculation of full production costs of Job no. IGI2014.

Particulars	Amount (₹)
Direct Materials	1,15,200
Direct Labour:	
- Fabrication Deptt. (240 hours × ₹ 18)	4,320
- Assembly Deptt. (180 hours × ₹ 18)	3,240
Production Overheads:	
- Fabrication Deptt. (210 hours × ₹ 3.60)	756
- Assembly Deptt. (180 hours × ₹ 1.22)	220
Total Production Cost	1,23,736

4. (i) **Calculation of Operating Cost per month for each vehicle**

	Ramgarh	Pratapgarh	Devgarh	Total
A. Running Costs:				
- Cost of diesel (Working Note- 2)	1,25,280	70,992	92,800	2,89,072
- Servicing cost (Working Note- 3)	9,000	---	3,000	12,000
	1,34,280	70,992	95,800	3,01,072
B. Fixed Costs:				
- Salary to drivers	72,000 (4 drivers × ₹ 18,000)	54,000 (3 drivers × ₹ 18,000)	90,000 (5 drivers × ₹ 18,000)	2,16,000
- Salary to cleaners	44,000 (4 cleaners × ₹ 11,000)	33,000 (3 cleaners × ₹ 11,000)	55,000 (5 cleaners × ₹ 11,000)	1,32,000
- Allocated garage parking fee	5,400 (4 vehicles × ₹ 1,350)	4,050 (3 vehicles × ₹ 1,350)	6,750 (5 vehicles × ₹ 1,350)	16,200
- Depreciation (Working Note- 4)	36,733	32,800	38,542	1,08,075
- Toll tax passes	2,850	3,020	---	5,870
	1,60,983	1,26,870	1,90,292	4,78,145
Total [A + B]	2,95,263	1,97,862	2,86,092	7,79,217
Operating Cost per vehicle	73,815.75 (₹ 2,95,263 ÷ 4 vehicles)	65,954 (₹ 1,97,862 ÷ 3 vehicles)	57,218.40 (₹ 2,86,092 ÷ 5 vehicles)	64,934.75 (₹ 7,79,217 ÷ 12 vehicles)

(ii) **Vehicle operating cost per litre of milk**

$$\frac{\text{Total Operating Cost per month}}{\text{Total milk carried a month}} = \frac{₹7,79,217}{1,47,00,000 \text{ Litres (Working Note} - 5)} = ₹\ 0.053$$

Working Notes:

1. **Distance covered by the vehicles in a month**

Route		Total Distance (in K.M.)
Ramgarh	(4 vehicles × 3 trips × 2 × 24 km. × 30 days)	17,280
Pratapgarh	(3 vehicles × 2 trips × 2 × 34 km. × 30 days)	12,240
Devgarh	(5 vehicles × 2 trips × 2 × 16 km. × 30 days)	9,600

2. Cost of diesel consumption

	Ramgarh	Pratapgarh	Devgarh
Total distance travelled (K.M.)	17,280	12,240	9,600
Mileage per litre of diesel	8 kmpl	10 kmpl	6 kmpl
Diesel consumption (Litre)	2,160 (17,280 ÷ 8)	1,224 (12,240 ÷ 10)	1,600 (9,600 ÷ 6)
Cost of diesel consumption @ ₹ 58 per litre (₹)	1,25,280	70,992	92,800

3. Servicing Cost

	Ramgarh	Pratapgarh	Devgarh
Total distance travelled (K.M.)	17,280	12,240	9,600
Covered under free service warranty	No	Yes	No
No. of services required	3 (17,280 k.m. ÷ 5,000 k.m.)	2 (12,240 k.m. ÷ 5,000 k.m.)	1 (9,600 k.m. ÷ 5,000 k.m.)
Total Service Cost (₹)	9,000 (₹ 3,000 × 3)	---	3,000 (₹ 3,000 × 1)

4. Calculation of Depreciation

	Ramgarh	Pratapgarh	Devgarh
No. of vehicles	4	3	5
Cost of a vehicle	11,02,000	13,12,000	9,25,000
Total Cost of vehicles	44,08,000	39,36,000	46,25,000
Depreciation per month	36,733 $\left(\frac{₹44,08,000 \times 10\%}{12 \text{ months}}\right)$	32,800 $\left(\frac{₹39,36,000 \times 10\%}{12 \text{ months}}\right)$	38,542 $\left(\frac{₹46,25,000 \times 10\%}{12 \text{ months}}\right)$

5. Total volume of Milk Carried

Route		Milk Qty. (Litre)
Ramgarh	(25,000 ltr. × 0.7 × 4 vehicles × 3 trips × 30 days)	63,00,000
Pratapgarh	(25,000 ltr. × 0.7 × 3 vehicles × 2 trips × 30 days)	31,50,000
Devgarh	(25,000 ltr. × 0.7 × 5 vehicles × 2 trips × 30 days)	52,50,000
		1,47,00,000

5. (a) Calculation of Total Cost for the Hostel Job

Particulars	Amount (₹)	Amount (₹)
Direct Material Cost:		
- 15mm GI Pipe (Working Note- 1)	11,051.28	
- 20mm GI Pipe (Working Note- 2)	2,588.28	
- Other fitting materials (Working Note- 3)	3,866.07	
- Stainless steel faucet 15 units × $\left(\frac{6 \times ₹204 + 15 \times ₹209}{21 \text{units}}\right)$	3,113.57	
- Valve 6 units × $\left(\frac{8 \times ₹404 + 10 \times ₹402 + 14 \times ₹424}{32 \text{units}}\right)$	2,472.75	23,091.95
Direct Labour:		
- Plumber [(180 hours × ₹ 50) + (12 hours × ₹ 25)]	9,300.00	
- Helper [(192 hours × ₹ 35) + (24 hours × ₹ 17.5)]	7,140.00	16,440.00
- Overheads [₹ 13 × (180 + 192) hours]		4,836.00
Total Cost		44,367.95

(b) Price to be charged for the job work:

	Amount (₹)
Total Cost incurred on the job	44,367.95
Add: 25% Profit on Job Price $\left(\frac{44,367.95}{75\%} \times 25\%\right)$	14,789.32
	59,157.27

Working Note:

1. Cost of 15mm GI Pipe

Date		Amount (₹)
17-08-2014	8 units × ₹ 600	4,800.00
28-08-2014	10 units × $\left(\frac{4 \times ₹600 + 35 \times ₹628}{39 \text{units}}\right)$	6,251.28
		11,051.28

2. Cost of 20mm GI Pipe

Date		Amount (₹)
12-08-2014	2 units × ₹ 660	1,320.00
28-08-2014	2 units × $\left(\frac{8 \times ₹\,660 + 30 \times ₹\,610 + 20 \times ₹\,660}{58\,\text{units}}\right)$	1,268.28
		2,588.28

3. Cost of Other fitting materials

Date		Amount (₹)
12-08-2014	18 units × ₹ 26	468.00
17-08-2014	30 units × ₹ 26	780.00
28-08-2014	34 units × $\left(\frac{12 \times ₹\,26 + 150 \times ₹\,28}{162\,\text{units}}\right)$	946.96
30-08-2014	60 units × $\left(\frac{12 \times ₹\,26 + 150 \times ₹\,28}{162\,\text{units}}\right)$	1,671.11
		3,866.07

6. Calculation of quantity produced

	Process- A (Ltr.)	Process- B (Ltr.)	Process- C (Ltr.)
Input	4,50,000	1,44,000	2,16,000
Normal Loss	(90,000)	(7,200)	(21,600)
	(20% of 4,50,000 ltr.)	(5% of 1,44,000 ltr.)	(10% of 2,16,000 ltr.)
	3,60,000	1,36,800	1,94,400
Production of Gasoline	1,44,000	136,800	--
Production of HSD	2,16,000	--	1,94,400

(i) Statement of apportionment of joint cost on the basis of sale value at split-off point

	Gasoline	HSD
Output at split-off point (Ltr.)	1,44,000	2,16,000
Selling price per Ltr. (₹)	64	41
Sales value (₹)	92,16,000	88,56,000
Share in Joint cost (128:123)	87,71,200	84,28,575
	$\left(\frac{₹1,71,99,775}{251} \times 128\right)$	$\left(\frac{₹1,71,99,775}{251} \times 123\right)$

(ii) Statement of cost per Litre.

	Gasoline	HSD
Output (Ltr.)	1,36,800	1,94,400
Share in joint cost (₹)	87,71,200	84,28,575
Cost per Ltr. (₹) (Joint cost)	64.11	43.36
Further processing cost (₹)	10,80,000	1,35,000
Further processing cost per Ltr. (₹)	7.89	0.69
Total cost per Ltr. (₹)	72.00	44.05

(iii) Statement of profit

	Gasoline	HSD
Output (Ltr.)	1,36,800	1,94,400
Sales (Ltr.)	1,32,000	1,88,000
Closing stock (Ltr.)	4,800	6,400
	(₹)	(₹)
Sales @ ₹68 and ₹46 for Gasoline and HSD respectively	89,76,000	86,48,000
Add: closing stock (Ltr.) (at full cost)	3,45,600	2,81,920
Value of production	93,21,600	89,29,920
Less: Share in joint cost	87,71,200	84,28,575
Further processing	10,80,000	1,35,000
Profit/ (Loss)	(5,29,600)	3,66,345

7. (i) Material Cost Variance = Standard Cost – Actual Cost

Or = SP × SQ – AP × AQ

A = (₹ 12,000 × 18 tonne × 0.74) – ₹ 1,62,000 = ₹ 2,160 (A)

B = (₹ 23,500 × 18 tonne × 0.40) – ₹ 1,65,200 = ₹ 4,000 (F)

C = (₹ 18,000 × 18 tonne × 0.64) – ₹ 2,07,000 = ₹ 360 (F)

= ₹ 2,200 (F)

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

Or = AQ × SP – AQ × AP

A = (13.12 tonne × ₹ 12,000) – ₹ 1,62,000

= ₹ 1,57,440 - ₹ 1,62,000 = ₹ 4,560 (A)

B = (7.1 tonne × ₹ 23,500) – ₹ 1,65,200

= ₹ 1,66,850 - ₹ 1,65,200 = ₹ 1,650 (F)

C = (11.5 tonne × ₹ 18,000) – ₹ 2,07,000

= ₹ 2,07,000 - ₹ 2,07,000 = Nil

= ₹ 2,910 (A)

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

Or = SP × SQ – SP × AQ

A = (₹12,000 × 18 tonne × 0.74) – (₹ 12,000 × 13.12 tonne)

= ₹ 1,59,840 – ₹ 1,57,440 = ₹ 2,400 (F)

B = (₹23,500 × 18 tonne × 0.40) – (₹ 23,500 × 7.10 tonne)

= ₹ 1,69,200 – ₹ 1,66,850 = ₹ 2,350 (F)

C = (₹18,000 × 18 tonne × 0.64) – (₹ 18,000 × 11.5 tonne)

= ₹ 2,07,360 – ₹ 2,07,000 = ₹ 360 (F)

= ₹ 5,110 (F)

(iv) Material Mix Variance = Std. Price (Revised Std. Quantity – Actual Quantity)

Or = SP × RSQ – SP × AQ

A = $\left(₹12{,}000 \times 31.72 \text{ tonne} \times \frac{0.74}{1.78}\right)$ – (₹ 12,000 × 13.12 tonne)

= ₹1,58,243.6 – ₹1,57,440 = ₹ 803.60 (F)

B = $\left(₹\ 23{,}500 \times 31.72 \text{ tonne} \times \frac{0.40}{1.78}\right)$ – (₹ 23,500 × 7.10 tonne)

= ₹ 1,67,510.11 – ₹1,66,850 = ₹ 660.11 (F)

C = $\left(₹18{,}000 \times 31.72 \text{ tonne} \times \frac{0.64}{1.78}\right)$) – (₹ 18,000 × 11.5 tonne)

= ₹ 2,05,288.99 – ₹ 2,07,000 = ₹ 1,711.01 (A)

= ₹ 2,47.30 (A)

(v) Material Yield Variance = Std. Price (Std. Quantity - Revised Std. Quantity)

Or = SP × SQ – SP × RSQ

A = (₹12,000 × 18 tonne × 0.74) - $\left(₹12{,}000 \times 31.72 \text{ tonne} \times \frac{0.74}{1.78}\right)$

= ₹1,59,840 - ₹1,58,243.6 = ₹ 1,596.40 (F)

B = (₹23,500 × 18 tonne × 0.40) - $\left(₹\ 23{,}500 \times 31.72 \text{ tonne} \times \frac{0.40}{1.78}\right)$

= ₹ 1,69,200 - ₹ 1,67,510.11 = ₹ 1,689.89 (F)

C = (₹18,000 × 18 tonne × 0.64) - $\left(₹18{,}000 \times 31.72 \text{ tonne} \times \frac{0.64}{1.78}\right)$

= ₹ 2,07,360 - ₹ 2,05,288.99 = ₹ 2,071.01 (F)

= ₹ 5,357.30 (F)

8. Calculation of Profit made in the month of August 2014 by selling 14,000 units.

	Amount per unit (₹)	Amount (₹)
Sales Revenue	18.00	2,52,000
Less: Variable Costs:		
- Direct Material	8.00	1,12,000
- Direct Labour	3.50	49,000
- Variable Overhead	2.50	35,000
Contribution	4.00	56,000
Less: Fixed Overhead	2.00	28,000
Profit	2.00	28,000

(i) To maintain the same amount of profit i.e. ₹ 28,000 in September 2014 also, the company needs to maintain a contribution of ₹ 56,000.

Let, number of units to be sold in September 2014 is 'x', then the contribution will be

₹ 18 x – [(₹8 × 1.10) + ₹ 3.5 + (₹ 2.5 × 1.05)] x = ₹ 56,000

₹ 18 x – (₹ 8.8 + ₹ 3.5 + ₹ 2.625) x = ₹ 56,000

Or, x $= \frac{₹\,56,000}{₹\,3.075}$

= 18,211.38 units or 18,212 units.

(ii) Margin of Safety

	August 2014	September 2014
Profit	₹ 28,000	₹ 28,000
P/V Ratio	$\frac{₹4}{₹18}\times 100$	$\frac{₹3.075}{₹18}\times 100$
Margin of Safety $\left(\frac{\text{Profit}}{\text{P / VRatio}}\times 100\right)$	₹1,26,000 $\left(\frac{28,000}{400}\times 18\times 100\right)$	₹1,63,902.44 $\left(\frac{28,000}{307.5}\times 18\times 100\right)$

9. (a) Preparation of Production Budget (in units)

	October	November	December	January
Demand for the month (Nos.)	4,000	3,500	4,500	6,000
Add: 20% of next month's demand	700	900	1,200	1,300
Less: Opening Stock	(950)	(700)	(900)	(1,200)
Vehicles to be produced	3,750	3,700	4,800	6,100

(b) Preparation of Purchase budget for Part-X

	October	November	December
Production for the month (Nos.)	3,750	3,700	4,800
Add: 40% of next month's production	1,480 (40% of 3,700)	1,920 (40% of 4,800)	2,440 (40% of 6,100)
	5,230	5,620	7,240
No. of units required for production	20,920 (5,230 × 4 units)	22,480 (5,620 × 4 units)	28,960 (7,240 × 4 units)
Less: Opening Stock	(4,800)	(5,920) (1,480 × 4 units)	(7,680) (1,920 × 4 units)
No. of units to be purchased	16,120	16,560	21,280

(c) Budgeted Gross Profit for the Quarter October to December

	October	November	December	Total
Sales in nos.	4,000	3,500	4,500	12,000
Net Selling Price per unit*	₹ 3,46,150	₹ 3,46,150	₹ 3,46,150	
Sales Revenue (₹ in lakh)	13,846	12,115.25	15,576.75	41,538
Less: Cost of Sales (₹ in lakh) (Sales unit × Cost per unit)	11,428	9,999.50	12,856.50	34,284
Gross Profit (₹ in lakh)	2,418	2,115.75	2,720.25	7,254

* Net Selling price unit = ₹ 3,95,600 – 12.5% commission on ₹ 3,95,600 = ₹ 3,46,150

10. (a) Cost Accounting is defined as "the process of accounting for cost which begins with the recording of income and expenditure or the bases on which they are calculated and ends with the preparation of periodical statements and reports for ascertaining and controlling costs."

The main objectives of the cost accounting are as follows:

(a) *Ascertainment of cost*: There are two methods of ascertaining costs, viz., Post Costing and Continuous Costing. Post Costing means, analysis of actual information as recorded in financial books. Continuous Costing, aims at collecting information about cost as and when the activity takes place so that as soon as a job is completed the cost of completion would be known.

(b) *Determination of selling price*: Business enterprises run on a profit making basis. It is thus necessary that the revenue should be greater than the costs incurred. Cost accounting provides the information regarding the cost to make and sell the product or services produced.

(c) *Cost control and cost reduction*: To exercise cost control, the following steps should be observed:

(i) Determine clearly the objective.

(ii) Measure the actual performance.

(iii) Investigate into the causes of failure to perform according to plan;

(iv) Institute corrective action.

(d) *Cost Reduction* may be defined "as the achievement of real and permanent reduction in the unit cost of goods manufactured or services rendered without impairing their suitability for the use intended or diminution in the quality of the product."

(e) *Ascertaining the profit of each activity*: The profit of any activity can be ascertained by matching cost with the revenue of that activity. The purpose under this step is to determine costing profit or loss of any activity on an objective basis.

(f) *Assisting management in decision making*: Decision making is defined as a process of selecting a course of action out of two or more alternative courses. For making a choice between different courses of action, it is necessary to make a comparison of the outcomes, which may be arrived under different alternatives.

(b) Reasons for disagreement of profits as per cost and financial accounts: The various reasons for disagreement of profits shown by the two sets of books viz., cost and financial may be listed as below:

1. *Items appearing only in financial accounts:* The following items of income and expenditure are normally included in financial accounts and not in cost accounts. Their inclusion in cost accounts might lead to unwise managerial decisions. These items are:

(i) Income:

(a) Profit on sale of assets

(b) Interest received

(c) Dividend received

(d) Rent receivable

(e) Share Transfer fees

(ii) Expenditure

(a) Loss on sale of assets

(b) Uninsured destruction of assets

(c) Loss due to scrapping of plan and machinery

(d) Preliminary expenses written off

(e) Goodwill written off

(f) Underwriting commission and debenture discount written off

(g) Interest on mortgage and loans

(h) Fines and penalties

(iii) Appropriation

(a) Dividends

(b) Reserves

(c) Dividend equalization fund, Sinking fund etc.

2. *Items appearing only in cost accounts:* There are some items which are included in cost accounts but not in financial account. These are:

(d) Notional interest on capital;

(e) Notional rent on premises owned.

3. *Under or over-absorption of overhead:* In cost accounts overheads are charged to production at pre-determined rates where in financial accounts actual amount of overhead is charged, the difference gives rise under or over-absorption; causing a difference in profits.

4. *Different bases of stock valuation:* In financial books, stocks are valued at cost or market price, whichever is lower. In cost books, however, stock of materials may be valued on FIFO or LIFO basis and work-in-progress may be valued at prime cost or works cost. Differences in store valuation may thus cause a difference between the two profits.

5. *Depreciation:* The amount of depreciation charge may be different in the two sets of books either because of the different methods of calculating depreciation or the rates adopted. In company accounts, for instance, the straight line method may be adopted whereas in financial accounts it may be the diminishing balance method.

(c) Cost plus contract: Under cost plus contract, the contract price is ascertained by adding a percentage of profit to the total cost of the work. Such types of contracts are entered into when it is not possible to estimate the contract cost with reasonable accuracy due to unstable condition of material, labour services etc.

Following are the advantages of cost plus contract:

(i) The contractor is assured of a fixed percentage of profit. There is no risk of incurring any loss on the contract.

(ii) It is useful specially when the work to be done is not definitely fixed at the time of making the estimate.

(iii) Contractee can ensure himself about the 'cost of contract' as he is empowered to examine the books and documents of the contractor to ascertain the veracity of the cost of contract.

(d) In some process industries the output of one process is transferred to the next process not at cost but at market value or cost plus a percentage of profit. *The difference between cost and the transfer price is known as inter-process profits.*

The advantages and disadvantages of using inter-process profit, in the case of process type industries are as follows:

Advantages:

1. Comparison between the cost of output and its market price at the stage of completion is facilitated.
2. Each process is made to stand by itself as to the profitability.

Disadvantages:

1. The use of inter-process profits involves complication.
2. The system shows profits which are not realised because of stock not sold out.

PART II: FINANCIAL MANAGEMENT

QUESTIONS

1. Answer the following, supporting the same with reasoning/working notes:

   (a) Discuss the risk-return considerations in financing of current assets.

   (b) Alpha Limited has ₹ 10 crores bonds outstanding. Bank deposits earn 10 per cent per annum. The bonds will be redeemed after 15 years for which purpose Alpha Limited wishes to create a sinking fund. How much amount should be deposited to the sinking fund each year so that Alpha Limited would have in the sinking fund ₹ 10 crores to retire its entire issue of bonds?

   (c) The overall cost of capital can be reduced by increasing the debt portion in the capital structure. Discuss.

   (d) Determine the present value of ₹ 700 each paid at the end of each of the next six years. Assume an 8 per cent of interest.

   (e) "Liquidity ratios are particularly useful in credit analysis by banks and other suppliers of short-term loans." Comment.

Management of Working Capital

2. Beta Limited faces an interest rate of 0.5 per cent per day and its broker charges ₹ 75 for each transaction in short-term securities. The managing director has stated that the minimum cash balance that is acceptable is ₹ 2,000 and that the variance of cash flows on a daily basis is ₹ 16,000. You are required to determine the maximum level of cash Beta Limited should hold and at what point should it start to purchase or sell securities?

Investment Decisions

3. Zeta Limited wants to replace its old machine with a new automatic machine. Two models A and B are available at the same cost of ₹ 5 lakhs each. Salvage value of the old machine is ₹ 1 lakh. The utilities of the existing machine can be used if the company purchases A. Additional cost of utilities to be purchased in that case are ₹ 1 lakh. If the company purchases B then all the existing utilities will have to be replaced with new utilities costing ₹ 2 lakhs. The salvage value of the old utilities will be ₹ 0.20 lakhs. The earnings after taxation are expected to be:

	(Cash inflows of)		
Year	*A* *₹*	*B* *₹*	*P.V. Factor* *@ 15%*
1.	1,00,000	2,00,000	0.87
2.	1,50,000	2,10,000	0.76
3.	1,80,000	1,80,000	0.66

4.	2,00,000	1,70,000	0.57
5.	1,70,000	40,000	0.50
Salvage Value at the end of Year 5	50,000	60,000	

The targeted return on capital is 15%. You are required to (i) Compute, for the two machines separately, net present value, discounted payback period and desirability factor and (ii) Advice which of the machines is to be selected ?

Financing Decisions

4. Gamma Limited has the following capital structure which is considered to be optimum as on 31st March, 2014.

	₹
14% Debentures	30,000
11% Preference shares	10,000
Equity (10,000 shares)	1,60,000
	2,00,000

The company share has a market price of ₹ 23.60. Next year dividend per share is 50% of year 2014 EPS. The following is the trend of EPS for the preceding 10 years which is expected to continue in future.

Year	*EPS (₹)*	*Year*	*EPS ₹)*
2005	1.00	2010	1.61
2006	1.10	2011	1.77
2007	1.21	2012	1.95
2008	1.33	2013	2.15
2009	1.46	2014	2.36

The company issued new debentures carrying 16% rate of interest and the current market price of debenture is ₹ 96.

Preference shares ₹ 9.20 (with annual dividend of ₹ 1.1 per share) were also issued. The company is in 50% tax bracket.

(a) Calculate after tax:

(i) Cost of new debt

(ii) Cost of new preference shares

(iii) New equity share (consuming new equity from retained earnings)

(b) Calculate marginal cost of capital when no new shares are issued.

(c) How much needs to be spent for capital investment before issuing new shares? 50% of the 2014 earnings are available as retained earnings for the purpose of capital investment.

(d) What will the marginal cost of capital when the funds exceed the amount calculated in (c), assuming new equity is issued at ₹ 20 per share?

Financing Decisions

5. Theta Limited has a total capitalization of ₹ 10 Lakhs consisting entirely of equity shares of ₹ 50 each. It wishes to raise another ₹ 5 lakhs for expansion through one of its two possible financial plans.

   (1) All equity shares of ₹ 50 each.

   (2) All debentures carrying 9% interest.

   The present level of EBIT is ₹ 1,40,000 and Income tax rate is 50%.

   Calculate EBIT level at which earnings per share would remain the same irrespective of raising funds through equity shares or debentures.

Financial Analysis and Planning

6. From the information provided by Sai Limited, you are required to prepare a statement of changes in working capital and the fund flow statement for the year.

Balance Sheet as at 31st March 2014 (All figures in Rupees)

Assets	2013	2014	Liabilities	2013	2014
	₹	₹		₹	₹
Current Assets			*Current Liabilities*		
Cash in Hand	10,000	2,000	Sundry Creditors	3,00,000	2,00,000
Bank Balances	20,000	8,000	Provision for Taxes	10,000	15,000
Sundry Debtors	2,10,000	1,80,000	Proposed Dividend	50,000	60,000
Stock	4,00,000	4,50,000			
Total Current Assets	6,40,000	6,40,000	Total Current Liabilities	3,60,000	2,75,000
Fixed Assets					
Fixed Assets	8,00,000	11,00,000			
Less: Accumulated Depreciation	1,60,000,	2,70,000			
Total Fixed Assets	6,40,000	8,30,000			
Other Assets			*Shareholder's Funds*		
Investments	1,60,000	6,70,000	Equity Share Capital	9,80,000	17,15,000

			General Reserves	1,00,000	1,50,000
Total Other Assets	1,60,000	6,70,000	Total Shareholders' Funds	10,80,000	18,65,000
Total Assets	14,40,000	21,40,000	Total Liabilities	14,40,000	21,40,000

It is also known that machinery costing ₹1,00,000 with an accumulated depreciation of ₹ 30,000 was sold for ₹60,000.

Investment Decisions

7. Mahalaxmi Limited, manufacturer of pressure cookers, is evaluating three investment situations: (1) produce a new line of aluminum skillets, (2) expand its existing pressure cooker line to include several new sizes, and (3) develop a new, higher-quality line of pressure cookers. If only the project in question is undertaken, the expected present values and the amounts of investment required are:

Project	*Investment required*	*Present value of Future Cashflows*
	₹	₹
1	2,00,000	2,90,000
2	1,15,000	1,85,000
3	2,70,000	4,00,000

If projects 1 and 2 are jointly undertaken, there will be no economies; the investments required and present values will simply be the sum of the parts. With projects 1 and 3, economies are possible in investment because one of the machines acquired can be used in both production processes. The total investment required for projects 1 and 3 combined is ₹ 4,40,000. If projects 2 and 3 are undertaken, there are economies to be achieved in marketing and producing the products but not in investment. The expected present value of future cash flows for projects 2 and 3 is ₹ 6,20,000. If all three projects are undertaken simultaneously, the economies noted will still hold. However, a ₹ 1,25,000 extension on the plant will be necessary, a space is not available for all three projects. Which project or projects should be chosen?

Financial Analysis and Planning

8. You have been hired as an analyst for the Bank of Delhi and your team is working on an independent assessment of Meyland Limited. Meyland Limited specializes in the production of freshly imported cheese from Switzerland. Your colleague has provided you with the following data for your reference:

Ratios	2014	2013	2012	2014 Industry Average
Long-term Debt	0.45	0.40	0.35	0.35

Inventory Turnover	62.65	42.42	32.25	53.25
Depreciation/Total Assets	0.25	0.014	0.018	0.015
Days' Sales in Receivables	113	98	94	130.25
Debt to Equity	0.75	0.85	0.90	0.88
Profit Margin	0.082	0.07	0.06	0.075
Total Asset Turnover	0.54	0.65	0.70	0.40
Quick Ratio	1.028	1.03	1.029	1.031
Current Ratio	1.33	1.21	1.15	1.25
Times Interest Earned	0.9	4.375	4.45	4.65
Equity Multiplier	1.75	1.85	1.90	1.88

(a) In the annual report to the shareholders, the CEO of Meyland Limited wrote, "2012 was a good year for the company with respect to our ability to meet our short-term obligations. We had higher liquidity largely due to an increase in highly liquid current assets (cash, account receivables and short-term marketable securities)." Is the CEO correct? Explain and use only relevant information in your analysis.

(b) What can you say about Meyland Limited's asset management? Be as complete as possible given the above information, but do not use any irrelevant information.

(c) You are asked to provide the shareholders with an assessment of Meyland Limited's solvency and leverage. Be as complete as possible given the above information, but do not use any irrelevant information.

Management of Working Capital

9. Lola Limited has a present annual sales turnover of ₹ 40,00,000. The unit sale price is ₹ 20. The variable cost are ₹ 12 per unit and fixed costs amount to ₹ 5,00,000 per annum. The present credit period of one month is proposed to be extended to either 2 or 3 months whichever will be more profitable. The following additional information is available:

	On the basis of Credit Period of		
	1 month	*2 months*	*3 months*
Increase in sales by	–	10%	30%
% of Bad debts to sales	1	2	5

Fixed cost will increase by ₹ 75,000 when sales will increase by 30%. The company requires a pre-tax return on investment at 20%.

Evaluate the profitability of the proposals and recommended best credit period for Lola Limited.

10. Answer the following:
    (a) Discuss Profitability Index (PI) as a tool of capital budgeting and give an illustration.
    (b) Differentiate between Global Depository Receipts and American Depository Receipts
    (c) Differentiate between Financial lease and Operating lease.

SUGGESTED ANSWERS / HINTS

1. (a) Risk-Return Considerations in Financing of Current Assets

The financing of current assets involves a trade off between risk and return. A firm can choose from short or long term sources of finance. Short term financing is less expensive than long term financing but at the same time, short term financing involves greater risk than long term financing.

Depending on the mix of short term and long term financing, the approach followed by a company may be referred as matching approach, conservative approach and aggressive approach.

In matching approach, long-term finance is used to finance fixed assets and permanent current assets and short term financing to finance temporary or variable current assets. Under the conservative plan, the firm finances its permanent assets and also a part of temporary current assets with long term financing and hence less risk of facing the problem of shortage of funds.

An aggressive policy is said to be followed by the firm when it uses more short term financing than warranted by the matching plan and finances a part of its permanent current assets with short term financing.

(b) Computation of Amount to be deposited in the Sinking Fund

$A = S_n/FVIFA_{i,\, n} = S_{15}$ = ₹10 Crore/$FVIFA_{10,\, 15}$ = ₹ 10 crore/31.772 = ₹ 3,14,742.54.

(c) "The overall cost of capital can be reduced by increasing the debt portion in the capital structure"

In a zero-tax environment, MM Hypothesis has proved that the overall cost of capital is independent of the amount of leverage in the capital structure. However, when companies are subject to tax, the overall cost of capital will be reduced due to the tax shield provided by debt.

(d) Computation of Present Value

Here, the present value of an annuity of ₹ 700 has to be computed. The present value factor of an annuity of Re. 1 at 8 per cent for 6 years is 4.623. Therefore, the present value of an annuity of ₹ 700 will be: 4.623× ₹ 700 = ₹ 3,236.10.

(e) "Liquidity ratios are particularly useful in credit analysis by banks and other suppliers of short-term loans"

The given statement is true because with the help of these ratios the stakeholders can draw conclusions regarding liquidity position of a firm. The liquidity position of a firm would be satisfactory, if it is able to meet its current obligations when they become due. Inability to pay-off short-term liabilities affects its credibility as well as its credit rating. Continuous default on the part of the business leads to commercial bankruptcy. Eventually such commercial bankruptcy may lead to its sickness and dissolution. Liquidity ratios are current ratio, liquid ratio and cash to current liability ratio.

2. The following steps may be followed for solving the problem:

(a) Determining of the lower level of cash Beta Limited is to have – this has been set at ₹ 2,000.

(b) Determining of the variation in cash flows of Beta Limited – this has been found to be ₹ 16,000.

(c) Calculation of the spread of transactions:

$$\text{Spread} = 3 \text{ x } \sqrt[3]{\frac{(0.75 \times \text{Variance of cashflow} \times \text{Transaction cost})}{\text{Interest rate}}}$$

$$\text{Spread} = 3 \text{ x } \sqrt[3]{\frac{(0.75 \times 16,000 \times 75}{0.005}}$$

= ₹ 1,694

(d) Calculation of the upper limit – this is the sum of the lower limit and the spread:

Upper limit : ₹ 2,000 + ₹ 1,694 = ₹ 3,694.

(e) Securities should be sold when the return point is reached. The return point is the sum of the lower limit and a third of the spread:

Return point = ₹ 2,000 + 1/3 (1,694) = ₹ 2,565.

Thus, Beta Limited is aiming for cash holding of ₹ 2,565 (return point). Therefore, if the balance of cash reaches ₹ 3,694 Beta Limited should buy ₹ 3,694 - ₹ 2,565 = ₹ 1,129 of marketable securities; if it falls to ₹ 2,000, then ₹ 2,565 - ₹ 2,000 = ₹ 565 of securities should be sold.

3. (i) Expenditure at year zero

(₹ in lakhs)

Particulars	*A*	*B*
Cost of Machine	5.00	5.00
Cost of Utilities	1.00	2.00
Salvage Value of Old Machine	(1.00)	(1.00)
Salvage Value of Old Utilities	–	(0.20)
Total Expenditure (Net)	5.00	5.80

(a) Discounted Value of Cash inflows *(₹ in lakhs)*

		Machine A		*Machine B*	
Year	*NPV Factor @ 15%*	*Cash inflows*	*Discounted Value of inflows*	*Cash flows*	*Discounted Value of inflows*
0	1.00	(5.00)	(5.00)	(5.80)	(5.80)
1	0.87	1.00	0.87	2.00	1.74
2	0.76	1.50	1.14	2.10	1.60
3	0.66	1.80	1.19	1.80	1.19
4	0.57	2.00	1.14	1.70	0.97
5	0.50	1.70	0.85	0.40	0.20
Salvage	0.50	0.50	0.25	0.60	0.30
Present Value			5.44		6.00
Net Present Value			0.44		0.20

(b) Discounted Payback Period *(₹ in lakhs)*

	Machine A		*Machine B*	
Year	*Discounted Cash inflows*	*Cumulative Discounted Cash inflows*	*Discounted Cash inflows*	*Cumulative Discounted Cash inflows*
0	(5.00)	—	(5.80)	—
1	0.87	0.87	1.74	1.74
2	1.14	2.01	1.60	3.34
3	1.19	3.20	1.19	4.53
4	1.14	4.34	0.97	5.50
5	1.10*	5.44	0.50*	6.00

* Includes salvage value

Discounted Payback Period (For A and B):

4 years + $\left(\frac{(0.66)}{1.10}\right)$ × 1 = 4.6 years   4 years + $\left(\frac{(0.30)}{0.50}\right)$ × 1 = 4.6 years

(c) Desirability Index

Profitability Index: $\frac{\text{Sum of present value of net cash inflow}}{\text{Initial cash outlay}}$

$\frac{₹\ 5.44 \text{ lakhs}}{₹\ 5.00 \text{ lakhs}}$ = 1.088 (A) $\frac{₹\ 6.00 \text{ lakhs}}{₹\ 5.80 \text{ lakhs}}$ = 1.034 (B)

(ii) Advise: The discounted payback period in both the cases is same, also the net present value is positive in both the cases but the desirability factor (profitability index) is higher in the case of Machine A, it is therefore better to choose Machine A.

4. (a) (i) Cost of New Debt

$$K_d = \frac{I(1-t)}{N}$$

$$= \frac{16(1-0.5)}{96} = 0.0833$$

(ii) Cost of New Preference Shares

$$K_p = \frac{P}{O}$$

$$= \frac{1.1}{9.2} = 0.12$$

(iii) Cost of New Equity Shares

$$K_e = \frac{D_1}{P_0} + G$$

$$= \frac{1.18}{23.60} + 0.10 = 0.05 + 0.10$$

= 0.15

Calculation of D_1

D_1 = 50% of 2014 EPS = 50% of 2.36 = ₹ 1.18

(b)

Type of Capital	*Proportion*	*Specific Cost*	*Product*
(1)	*(2)*	*(3)*	*(2) × (3) = (4)*
Debt	0.15	0.0833	0.0125
Preference	0.05	0.12	0.0060
Equity	0.80	0.15	0.1200
	Marginal Cost of Capital		0.1385

(c) The company can spend the following amount:

Retained earnings = (0.50) (2.36 × 10,000) = ₹ 11,800

The ordinary equity is 80% of total capital

$$\text{Capital investment} = \frac{₹\,11,800}{0.80} = ₹\,14,750$$

(d) If the company requires funds in excess of ₹ 14,750 it will have to issue new shares.

The cost of new issue will be

$$K_e = \frac{₹\,1.18}{20} + 0.10 = 0.159$$

The marginal cost of capital will be

Type of Capital	*Proportion*	*Specific Cost*	*Product*
(1)	*(2)*	*(3)*	*(2) × (3) = (4)*
Debt	0.15	0.0833	0.0125
Preference	0.05	0.1200	0.0060
Equity (New)	0.80	0.1590	0.1272
			0.1457

5. Computation of Level of EBIT where EPS will be Equal for Both Alternatives

The level of EBIT where EPS will be equal under both the alternatives can be ascertained by the following equation:

$$= \frac{(X - Int_1)(1 - T)}{S_1} = \frac{(X - Int_2)(1 - T)}{S_2}$$

In Alternative 1, there will be no fixed interest liability, Equity shares= 20,000+10,000=30,000.

In Alternative 2, debentures of ₹ 5 lakhs carrying 9% interest will be used. Debentures interest will be:

$$\frac{9 \times 5,00,000}{100} = ₹\ 45,000$$

Substituting the values in the above equation:

$$\frac{(X - 0)(1 - 0.5)}{30,000} = \frac{(X - 45,000)(1 - 0.5)}{20,000}$$

or

X = 1,35,000

At EBIT level of ₹ 1,35,000 earnings per share in both cases will be equal:

Calculation of EPS

	Alternative 1	*Alternative 2*
Equity Shares (A)	30,000	20,000
Debentures	0	₹ 5,00,000
	₹	₹
EBIT	1,35,000	1,35,000
Interest	0	45,000
	1,35,000	90,000
Less: Income Tax @ 50%	67,500	45,000
Earnings after Tax (B)	67,500	45,000

$$\text{EPS} = \frac{B}{A} = 2.25$$

6. Statement of Changes in Working Capital (All figures in Rupees)

Particulars	*2013*	*2014*	*Increase in Working Capital*	*Decrease in Working Capital*
Current Assets				
Closing Stock	4,00,000	4,50,000	50,000	
Sundry Debtors	2,10,000	1,80,000		30,000
Cash in Hand	10,000	2,000		8,000
Bank Balance	20,000	8,000		12,000
Total(A)	6,40,000	6,40,000		

Current Liabilities				
Sundry Creditors	3,00,000	2,00,000	1,00,000	
Provision for Taxes	10,000	15,000		5,000
Proposed Dividends	50,000	60,000		10,000
Total(B)	3,60,000	2,75,000		
Working Capital (A)-(B)	2,80,000	3,65,000		
Increase in Working Capital	85,000			85,000
	3,65,000	3,65,000	1,50,000	1,50,000

Now, before preparing the funds from operation statement and the funds flow statement, we have to calculate the amount of depreciation charged for the year and also the amount of profit or loss on account of sale of machinery. For this, we need to prepare a machinery account in the following manner:

Machinery A/c

Particulars	₹
Balance of Fixed Assets as at 2013	8,00,000
Less: Cost of Machinery sold	1,00,000
Balance in fixed assets group after sale	7,00,000
Amount of Fixed assets as at 2014	11,00,000
Difference being additional purchase in Year	4,00,000

The written down value of the machinery is the cost minus the accumulated depreciation up to the point of sale. The sale price of the machinery, minus the written down value of the machinery sold, was ₹ 60,000 - [₹ 100,000-₹ 30,000]. Loss on sale of machinery comes to ₹ 10,000.

Based upon the same logic, we have to calculate the amount of depreciation for the year.

Depreciation A/c

Particulars	₹
Opening Balance of Accumulated Depreciation	1,60,000
Less: Accumulated depreciation of machinery sold	30,000
Balance in the accumulated depreciation account	1,30,000
Closing balance as on 2014	2,70,000
Difference being depreciation for the year	1,40,000

Funds from Operations for the Year 2014

Particulars	₹
Profit for the Year (Increase in General reserves)	50,000
Add: Depreciation	1,40,000
Non-operational activity (loss on machine)	10,000
Fund From Operations	2,00,000

Funds Flow Statement for the Year 2014

Particulars	₹
Sources	
Funds from Operation	2,00,000
Proceeds from Sale of Machinery	60,000
Proceeds from Issue of Shares	7,35,000
Total (A)	9,95,000
Applications	
Purchase of Machinery	4,00,000
Purchase of Investment	5,10,000
Increase in Working Capital	85,000
Total (B)	9,95,000

7. Computation of Net Present Value (NPV) and Advise to Mahalaxmi Limited

Project	*Investment Required*	*Present value of Future Cash Flows*	*Net Present value*
	₹	₹	₹
1	2,00,000	2,90,000	90,000
2	1,15,000	1,85,000	70,000
3	2,70,000	4,00,000	1,30,000
1 and 2	3,15,000	4,75,000	1,60,000
1 and 3	4,40,000	6,90,000	2,50,000
2 and 3	3,85,000	6,20,000	2,35,000
1, 2 and 3	6,80,000	9,10,000	2,30,000

Advise: *Projects 1 and 3 should be chosen, as they provide the highest net present value.*

8. (a) The answer should be focused on using the current and quick ratios. While the current ratio has steadily increased, it is to be noted that the liquidity has not

resulted from the most liquid assets as the CEO proposes. Instead, from the quick ratio, it is noted that the increase in liquidity is caused by an increase in inventories. For a fresh cheese company, it can be argued that inventories are relatively liquid when compared to other industries. Also, given the information, the industry-benchmark can be used to derive that the company's quick ratio is very similar to the industry level and that the current ratio is indeed slightly higher - again, this seems to come from inventories.

(b) Inventory turnover, day’s sales in receivables, and the total asset turnover ratio are to be mentioned here. Inventory turnover has increased over time and is now above the industry average. This is good - especially given the fresh cheese nature of the company’s industry. In 2014, it means for example that every 365/62.65 = 5.9 days the company is able to sell its inventories as opposed to the industry average of 6.9 days. Days' sales in receivables have gone down over time, but are still better than the industry average. So, while they are able to turn inventories around quickly, they seem to have more trouble collecting on these sales, although they are doing better than the industry. Finally, total asset turnover is gone down over time, but it is still higher than the industry average. It does tell us something about a potential problem in the company's long term investments, but again, they are still doing better than the industry.

(c) Solvency and leverage is captured by an analysis of the capital structure of the company and the company's ability to pay interest. Capital structure: Both the equity multiplier and the debt-to-equity ratio tell us that the company has become less levered. To get a better idea about the proportion of debt in the firm, we can turn the D/E ratio into the D/V ratio: 2014: 43%, 2013: 46%, 2012:47%, and the industry-average is 47%. So based on this, we would like to know why this is happening and whether this is good or bad. From the numbers it is hard to give a qualitative judgment beyond observing the drop in leverage. In terms of the company's ability to pay interest, 2014 looks pretty bad. However, remember that times interest earned uses EBIT as a proxy for the ability to pay for interest, while we know that we should probably consider cash flow instead of earnings. Based on a relatively large amount of depreciation in 2014 (see info), it seems that the company is doing just fine.

9. Evaluation of Profitability under different Credit Periods

(₹ in Lakhs)

	Particulars	*1 Month*	*2 Months*	*3 Months*
A.	Expected profit :			
	(a) Sales	40,00,000	44,00,000	52,00,000
	(b) Total Cost:			

	(i) Variable Cost @ ₹12	24,00,000	26,40,000	31,20,000
	(ii) Fixed Costs	5,00,000	5,00,000	5,00,000
		29,00,000	31,40,000	36,20,000
	(c) Expected Profit	11,00,000	12,60,000	15,80,000
B.	Opportunity Cost of Investment in Receivables	48,333	1,04,667	1,81,000
C.	Net Benefits [A-B]	10,51,667	11,55,333	13,99,000

Recommendation: *The credit period (i.e. 3 months) should be adopted since the net benefits under this policy are higher than those under other policies.*

Working Note

Calculation of Opportunity Cost of Investments in Receivables:

Opportunity Cost $= \text{Total Cost} \times \frac{\text{Collection Period}}{360} \times \frac{\text{Rate of Return}}{100}$

1 Month $= ₹\ 29,00,000 \times \frac{1}{12} \times \frac{20}{100} = ₹\ 48,333$

2 Months $= ₹\ 31,40,000 \times \frac{2}{12} \times \frac{20}{100} = ₹1,04,667$

3 Months $= ₹\ 36,20,000 \times \frac{3}{12} \times \frac{20}{100} = ₹1,81,000$

10. (a) Profitability index: In capital budgeting, there are cases when we have to compare or rank a number of proposals each involving different amount of cash flows. One of the methods of comparing/ranking such proposal is to work out what is known as profitability index (PI). It is also called benefit-cost ratio. It may be calculated as follows:

$$PI = \frac{\text{Present value of net cash inflows}}{\text{Initial cash outlay}}$$

Suppose, for example a company is considering two projects viz., A and B. The present value of net cash flows and initial outlay are as follows:

	Project A ₹	*Project B* ₹
Present Value of Net Cash Inflows	36,000	34,000
Initial Cash Outlay	30,000	29,000

In the case of the example, Project A has profitability index of 1.20 whereas Project B's ratio is 1.17 calculated as under:

$$A = \frac{₹\ 36,000}{₹\ 30,000} = 1.20$$

$$B = \frac{₹\ 34,000}{₹\ 29,000} = 1.17$$

It may be noted that as long as the profitability index is equal to or greater than 1.00, the project is acceptable.

Alternatively, profitability index may also be calculated as under:

$$PI = \frac{\text{Sum of discounted cash inflows}}{\text{Sum of discounted cash outlfows}}.$$

(b) Differentiation between Global Depository Receipts (GDRs) and American Depository Receipts (ADRs)

Global Depository Receipts (GDRs) is a negotiable certificate denominated in US dollars, which represents a-non-US companies publicly, traded local currency equity. GDRs are created when the local currency shares of an Indian company are delivered to the depository's local custodian bank, against which depository bank issues depository receipts in US dollar.

They may be freely traded in the overseas market like any other dollar denominated security either on a foreign stock exchange or in the over the counter market of qualified institutional buyers (QIBs). By issue of GDRs, Indian companies are able to tap global equity market to raise foreign currency funds by way of equity. It has distinct advantage over debt as there is no repayment of the principal and service costs are lower.

Whereas, American Depository Receipts (ADRs) are depository receipts issued by a company in the USA and are governed by the provisions of Security and Exchange Commission of USA. As the regulations are severe, Indian Companies tap the American market through private debt placements of GDRs listed in London and Luxemburg Stock Exchanges. Apart from legal impediments, ADRs are costlier than GDR Legal fees are considerably high for US listing. Registration fee in USA is also substantial. Hence, ADRs are less popular than GDRs.

(c) Difference between Financial Lease and Operating Lease

	Financial Lease	Operating Lease
1.	The risk and reward incident to ownership are passed on the lessee. The lessor only remains	The lessee is only provided the use of the asset for a certain time. Risk incident to ownership belongs only to

	the legal owner of the asset.	the lessor.
2	The lessee bears the risk of obsolescence.	The lessee is only allowed the use of asset.
3	The lease is non-cancellable by either party under it.	The lease is kept cancellable by the lessor.
4.	The lessor does not bear the cost of repairs, maintenance or operations.	Usually, the lessor bears the cost of repairs, maintenance or operations.
5.	The lease is usually full payout.	The lease is usually non-payout.

PAPER – 4: TAXATION

PART – I : STATUTORY UPDATE

Significant Notifications in income-tax and indirect taxes issued between 1st May 2013 and 30th April, 2014

A. INCOME TAX

NOTIFICATIONS

1. Notification No. 39/2013 dated 31.05.2013

Time and mode of payment of tax deducted at source under section 194-IA to the credit of Central Government, furnishing challan-cum-statement and TDS Certificate [Rules 30, 31A & 31]

New section 194-IA has been inserted by the Finance Act, 2013, requiring every transferee responsible for paying any sum as consideration for transfer of immovable property (land, other than agricultural land, or building or part of building) to deduct tax, at the rate 1% of such sum, at the time of credit of such sum to the account of the resident transferor or at the time of payment of such sum to a resident transferor, whichever is earlier.

Accordingly, the time and mode of, payment of tax deducted at source under section 194-IA, furnishing challan-cum-statement and TDS Certificate have been provided, by amending Rules 30, 31A & 31, respectively -

(i) Such sum deducted under section 194-IA shall be paid to the credit of the Central Government within a period of seven days from the end of the month in which the deduction is made and shall be accompanied by a challan-cum-statement in Form No.26QB *[Rule 30].*

(ii) The amount so deducted has to be deposited to the credit of the Central Government by electronic remittance within the above mentioned time limit, into RBI, SBI or any authorized bank *[Rule 30]*.

(iii) Every person responsible for deduction of tax under section 194-IA shall furnish to the DGIT (Systems) or any person authorized by him, a challan-cum-statement in Form No.26QB electronically within seven days from the end of the month in which the deduction is made *[Rule 31A]*.

(iv) Every person responsible for deduction of tax under section 194-IA shall furnish the TDS certificate in Form No.16B to the payee within 15 days from the due date for furnishing the challan-cum-statement in Form No.26QB under Rule 31A, after generating and downloading the same from the web portal specified by the DGIT (Systems) or the person authorized by him *[Rule 31]*.

2. Notification No. 40/2013 dated 6.06.2013

Notification of Cost Inflation Index for F.Y.2013-14

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

Accordingly, the Central Government has, in exercise of the powers conferred by clause (v) of *Explanation* to section 48, specified the Cost Inflation Index for the financial year 2013-14 as 939.

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

3. Notification No. 64/2013, dated 19.08.2013

Notification of foreign company for claiming exemption under section 10(48)

Income received by a foreign company in India in Indian currency from sale of crude oil, any other goods or rendering of services, as may be notified by the Central Government in this behalf, to any person in India is exempt under section 10(48). For this purpose, the foreign company, as well as the arrangement or agreement, should be notified by the Central Government having regard to the national interest. The foreign company should not be engaged in any other activity in India, except receipt of income under such arrangement or agreement.

Accordingly, vide this notification, the Central Government, having regard to the national interest, has notified for the purposes of the said clause, the National Iranian Oil Company, as the foreign company and the Memorandum of Understanding entered into between the Government of India in the Ministry of Petroleum and Natural Gas and the Central Bank of Iran on 20th January, 2013, as the agreement subject to the condition that the said foreign company shall not engage in any activity in India, other than the receipt of income under the agreement aforesaid.

The Notification is deemed to be effective from 20th January, 2013.

4. **Notification No.79/2013 dated 07.10.2013**

Reverse Mortgage Scheme amended to include within its scope, disbursement to an annuity sourcing institution for periodic payments by way of annuity to the Reverse Mortgagor

The Central Government had notified the Reverse Mortgage Scheme, 2008 in exercise of the powers conferred by clause (xvi) of section 47 of the Income-tax Act, 1961. Reverse Mortgage means mortgage of a capital asset by an eligible person against a loan obtained by him from an approved lending institution. Such kind of a transaction is not regarded as transfer under section 47(xvi) and amounts received by the Reverse Mortgagor as loan, either in lump-sum or in installment, are exempt under section 10(43).

The Central Government has, vide this notification, amended the Reverse Mortgage Scheme, 2008, to include within its scope, disbursement of loan by an approved lending institution, in part or in full, to the annuity sourcing institution, for the purposes of periodic payments by way of annuity to the reverse mortgagor. This would be an additional mode of disbursement, i.e., in addition to direct disbursements by the approved lending institution to the Reverse Mortgagor by way of periodic payments or lump sum payment in one or more tranches.

An annuity sourcing institution has been defined to mean Life Insurance Corporation of India or any other insurer registered with the Insurance Regulatory and Development Authority.

Maximum Period of Reverse Mortgage Loan

	Mode of disbursement	Maximum period of loan
(a)	Where the loan is disbursed directly to the Reverse Mortgagor	20 years from the date of signing the agreement by the reverse mortgagor and the approved lending institution.
(b)	Where the loan is disbursed, in part or in full, to the annuity sourcing institution for the purposes of periodic payments by way of annuity to the Reverse Mortgagor	The residual life time of the borrower.

5. Notification No. 94/2013, dated 18.12.2013

Notification of "Rajiv Gandhi Equity Savings Scheme, 2013" for the purpose of deduction under section 80CCG

The Finance Act, 2012 had inserted section 80CCG in the Income-tax Act, 1961 to provide for a one-time deduction for A.Y.2013-14 to a resident individual who acquires listed equity shares in a previous year in accordance with a scheme notified by the Central Government, to encourage flow of savings in financial instruments and improve the depth of domestic capital market. However, only a resident individual, being a new retail investor, whose gross total income did not exceed ₹ 10 lakh was eligible for the benefit of deduction. The deduction was 50% of amount invested in such equity shares or ₹ 25,000, whichever is lower. The maximum deduction of ₹ 25,000 was available on investment of ₹ 50,000 in such listed equity shares.

The Finance Act, 2013 has amended the provisions of section 80CCG w.e.f. A.Y.2014-15 so that the benefit of deduction under this section is available to a new retail investor, being a resident individual with gross total income of up to **₹ 12 lakh**, for investment in listed equity shares **or listed units of equity oriented fund**, in accordance with a notified scheme. Further, the deduction shall be allowed **for three consecutive assessment years**, beginning with the assessment year relevant to the previous year in which the listed equity shares or listed units of equity oriented fund were first acquired. The quantum of deduction would continue to remain the same.

Accordingly, the Central Government has, in exercise of the powers conferred by section 80CCG(1), notified the Rajiv Gandhi Equity Savings Scheme, 2013. The said scheme provides for eligibility criteria, procedure for investment, period of holding and other conditions.

S.No.	Particulars	Content
1.	**Eligibility**	The deduction under this scheme shall be available to a **new retail investor** who complies with the conditions of the Scheme and whose gross total income for the financial year in which the investment is made under the Scheme is less than or equal to₹ 12 lakh. **New retail investor** means a resident individual,: (i) **who has not opened a demat account** and has not made any transactions in the derivative segment before – - the date of opening of a demat account; or - the first day of the **initial year**, whichever is later However, an individual who is not the first account holder of an existing

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<td>joint demat account shall be deemed to have not opened a demat account for the purposes of this Scheme;
(ii) who has opened a demat account but has not made any transactions in the equity segment or the derivative segment before –
- the date he designates his existing demat account for the purpose of availing the benefit under the Scheme; or
- the first day of the initial year.</td>
<td>whichever is later</td>
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<td>Initial year means -
(a) the financial year in which the investor designates his demat account as Rajiv Gandhi Equity Savings Scheme account and makes investment in the eligible securities for availing deduction under the Scheme; or
(b) the financial year in which the investor makes investment in eligible securities for availing deduction under the Scheme for the first time, if the investor does not make any investment in eligible securities in the financial year in which the account is so designated.</td>
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<td>2.</td>
<td>Procedure for investment under the Scheme</td>
<td>A new retail investor shall make investments under the Scheme in the following manner, namely:-
1. the new retail investor may invest in one or more financial years in a block of three consecutive financial years beginning with the initial year;
2. the new retail investor may make investment in eligible securities in one or more than one transaction during any financial year during the three consecutive financial years beginning with the initial year in which the deduction has to be claimed;
3. the new retail investor may make any amount of investment in the demat account but the amount eligible for deduction under the Scheme shall not exceed fifty thousand rupees in a financial year;</td>
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<tr><td></td><td></td><td>4. the new retail investor shall be eligible for the tax benefit under the Scheme only for three consecutive financial years beginning with the initial year, in respect of the investment made in each financial year;
5. if the new retail investor does not invest in any financial year following the initial year, he may invest in the subsequent financial year, within the three consecutive financial years beginning with the initial year, in accordance with the Scheme;
6. the new retail investor who has claimed a deduction under sub-section (1) of section 80CCG of the Act in any assessment year shall not be allowed any deduction under the Scheme for the same investment for any other assessment year;
7. the new retail investor shall be permitted a grace period of seven trading days from the end of the financial year so that the eligible securities purchased on the last trading day of the financial year also get credited in the demat account and such securities shall be deemed to have been acquired in the financial year itself;
8. the new retail investor can make investments in securities other than the eligible securities covered under the Scheme and such investments shall not be subject to the conditions of the Scheme nor shall they be counted for availing the benefit under the Scheme;
9. the deduction claimed shall be withdrawn if the lock-in period requirements of the investment are not complied with or any other condition of the Scheme is contravened by the new retail investor.</td></tr>
<tr><td>3.</td><td>Period of holding</td><td>The period of holding of eligible securities invested in each financial year shall be under a lock-in period of three years to be counted in the following manner:
<table>
<tr><th>Type of lock-in</th><th>Meaning</th><th>Condition</th></tr>
<tr><td>Fixed lock-in period</td><td>The period commencing from the date of purchase of eligible securities in the relevant financial year and ending on 31st March of the year</td><td>The new retail investor shall hold eligible securities for fixed lock-in period. He shall not be permitted to sell, pledge or hypothecate any eligible security during the fixed lock-in</td></tr>
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			immediately following the relevant financial year.	period.
		Flexible lock-in period	The period of two years beginning immediately after the end of the fixed lock-in period shall be called the flexible lock-in period.	The new retail investor shall be permitted to trade the eligible securities after the completion of the fixed lock-in period subject to the conditions prescribed under the scheme. The demat account should be compliant for a cumulative period of a minimum of 270 days during each of the two years of the flexible lock-in period. The demat account shall be considered as compliant for the number of days for which the value of the investment portfolio of eligible securities (other than those which are in fixed lock-in) is equal to or higher than the corresponding investment claimed as eligible for the purpose of deduction under section 80CCG.
4.	Other Conditions	(i) While making initial investments up to ₹ 50,000, the total cost of acquisition of eligible securities shall not include brokerage charges, securities transaction tax, stamp duty, service tax and any other tax, which may appear in the contract note. (ii) Where the investment of the new retail investor undergoes a change as a result of involuntary corporate actions including demerger of companies, amalgamation and such other actions, as may be notified by SEBI, resulting in debit or credit of securities		

		covered under the Scheme, the deduction claimed by such investor shall not be affected. (iii) In the case of voluntary corporate actions, including buy-back resulting only in debit of securities where new retail investor has the option to exercise his choice, the same shall be considered as a sale transaction for the purpose of the Scheme.
5.	Consequence of failure to comply with the prescribed conditions	If the new retail investor fails to fulfill any of the provisions of the Scheme, the deduction originally allowed to him under section 80CCG(1) for any previous year, shall be deemed to be the income of the assessee of the previous year in which he fails to comply with the provisions of the Scheme and shall be liable to tax for the assessment year relevant to such previous year.
6.	Savings	A new retail investor who has invested in accordance with the Rajiv Gandhi Equity Savings Scheme, 2012 shall continue to be governed by the provisions of that Scheme to the extent it is not in contravention of the provisions of this Scheme and such investor shall also be eligible for the benefit of investment made in accordance with this Scheme for the financial years 2013-14 and 2014-15.

6. Notification No.6/2014 dated 15.01.2014

Contributory Health Service Scheme of the Department of Space notified under section 80D

Section 80D(2)(a) provides for deduction in respect of medical insurance premium paid or for contribution made by an individual to the Central Government Health Scheme or such other scheme as may be notified by the Central Government. Accordingly, the Central Government has notified the Contributory Health Service Scheme of the Department of Space, contribution to which would be eligible for deduction under section 80D.

Therefore, any contribution made by an individual towards the Contributory Health Service Scheme of the Department of Space would be eligible for deduction under section 80D, subject to the overall limit of ₹ 15,000 or ₹ 20,000, as the case may be.

CIRCULARS

1. Circular No.10/2013, dated 16.12.2013

Disallowance of interest etc. paid to a resident at any time during the previous year without deduction of tax under section 40(a)(ia)

Section 40(a)(ia) provides for disallowance of any interest, commission or brokerage, rent, royalty, fees for professional services or fees for technical services payable to a resident, or amounts payable to a contractor or sub-contractor, being resident, for carrying out any work (including supply of labour for carrying out any work), on which tax is deductible at source under Chapter XVII-B and such tax has not been deducted or, after deduction, has not been paid on or before the due date specified in section 139(1).

There have been conflicting interpretations by judicial authorities regarding the applicability of provisions of section 40(a)(ia), with regard to the amount not deductible in computing the income chargeable under the head 'Profits and gains of business or profession'. Some court rulings have held that the provisions of disallowance under section 40(a)(ia) apply only to the amount which remained payable at the end of the relevant financial year and would not be invoked to disallow the amount which had actually been paid during the previous year without deduction of tax at source.

Departmental View: The CBDT's view is that the provisions of section 40(a)(ia) would cover not only the amounts which are payable as on 31st March of a previous year but also amounts which are payable at any time during the year. The statutory provisions are amply clear and in the context of section 40(a)(ia), the term "payable" would include "amounts which are paid during the previous year".

The Circular has further clarified that where any High Court decides an issue contrary to the above "Departmental View", the "Departmental View" shall not be operative in the area falling in the jurisdiction of the relevant High Court.

2. **Circular No. 1/2014, dated 13.1.2014**

Non-deduction of tax at source on the service tax component comprised in payments made to residents, if the service-tax component is indicated separately

The CBDT had issued Circular No.4/2008 dated 28.4.2008 clarifying that tax is to be deducted at source under section 194-I, on the amount of rent paid/payable without including the service tax component. However, this Circular was silent regarding deduction of tax at source on the service tax component of other payments on which TDS provisions are applicable.

Accordingly, in exercise of the powers conferred under section 119, the Board has, vide this Circular, clarified that wherever in terms of the agreement/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 under Chapter XVII-B on the amount paid/payable without including such service tax component.

3. **Circular No. 2/2014 dated 20.01.2014**

Taxability of Awards received by a Sportsman

The CBDT had issued Circular No.447 on 22nd January, 1986 clarifying that awards received by a sportsman, who is not a professional, will not be liable to tax in his hands as the award will be in the nature of a gift and/or personal testimonial. This circular was applicable when the gift was not taxable in the hands of the recipient. Thereafter, in the year 2005, there was a fundamental change in the manner of treatment of gift through insertion of sub-clauses (xiii), (xiv) and (xv) of section 2(24). Corresponding amendments were also made in section 56(2) by insertion of clauses (v), (vi) and (vii), thereby making an amount of money or immovable property received without consideration taxable subject to provisions of these clauses. Consequently, the CBDT has, through this Circular, clarified that Circular No.447 had become inapplicable w.e.f. 1-4-2005, since the statutory provisions have overridden the same.

It may however be noted that, in terms of provisions of section 10(17A), Central Government approves awards instituted by Central Government, State Government or other bodies as also the purposes for rewards instituted by Central Government or State Government from time to time. Tax exemption can be sought by eligible persons in respect of awards or rewards covered by such approvals.

4. Circular No. 5/2014, dated 11.2.2014

Clarification regarding disallowance of expenses under section 14A in cases where corresponding exempt income has not been earned during the financial year

The Finance Act, 2001 had introduced section 14A, with retrospective effect from 1st April, 1962, to provide that no deduction shall be allowed in respect of expenditure incurred relating to income which does not form part of total income. A controversy has arisen as to whether disallowance can be made by invoking section 14A even in those cases where no income has been earned by an assessee, which has been claimed as exempt during the financial year.

The CBDT has, through this Circular, clarified that the legislative intent is to allow only that expenditure which is relatable to earning of income. Therefore, it follows that the expenses which are relatable to earning of exempt income have to be considered for disallowance, irrespective of the fact whether such income has been earned during the financial year or not.

The above position is clarified by the usage of the term "includible" in the heading to section 14A [Expenditure incurred in relation to income not includible in total income] and Rule 8D [Method for determining amount of expenditure in relation to income not includible in total income], which indicates that it is not necessary that exempt income should necessarily be included in a particular year's income, for triggering disallowance. Also, the terminology used in section 14A is "income under the Act" and not "income of the year", which again indicates that it is not material that the assessee should have earned such income during the financial year under consideration.

In effect, section 14A read along with Rule 8D provides for disallowance of expenditure even where the taxpayer has not earned any exempt income in a particular year.

5. Circular No. 8/2014 dated 31.03.2014

Taxability of partner's share, where the income of the firm is exempt under Chapter III / deductible under Chapter VI-A

Section 10(2A) provides that a partner's share in the total income of a firm which is separately assessed as such shall not be included in computing the total income of the partner. In effect, a partner's share of profits in such firm is exempt from tax in his hands.

Sub-section (2A) was inserted in section 10 by the Finance Act, 1992 with effect from 1.4.1993 consequent to change in the scheme of taxation of partnership firms. Since A.Y.1993-94, a firm is assessed as such and is liable to pay tax on its total income. A partner is, therefore, not liable to tax once again on his share in the said total income.

An issue has arisen as to the amount which would be exempt in the hands of the partners of a partnership firm, in cases where the firm has claimed exemption/deduction under Chapter III or Chapter VI-A.

The CBDT has clarified that the income of a firm is to be taxed in the hands of the firm only and the same can under no circumstances be taxed in the hands of its partners. Therefore, the entire profit credited to the partners' accounts in the firm would be exempt from tax in the hands of such partners, even if the income chargeable to tax becomes Nil in the hands of the firm on account of any exemption or deduction available under the provisions of the Act.

B. INDIRECT TAXES

CENTRAL EXCISE

Following amendments have been carried out in the CENVAT Credit Rules, 2004:

1. **Procedure, safeguards, conditions and limitations prescribed for refund of CENVAT credit to service providers covered under partial reverse charge**

   Rule 5B stipulates that a service provider providing services taxed under reverse charge mechanism and unable to utilize the CENVAT credit availed on inputs and input services for payment of service tax on such output services, shall be allowed refund of such unutilized CENVAT credit.

   The procedure, safeguards, conditions and limitations to which such refund shall be subject to have been prescribed by CBEC vide *Notification No. 12/2014 CE (NT) dated 03.03.2014* as under:

   I. SAFEGUARDS, CONDITIONS AND LIMITATIONS

   (a) Refund is admissible, of unutilised CENVAT credit taken on inputs and input services during the half year for which refund is claimed, for providing following output services:

   (i) renting of a motor vehicle designed to carry passengers on non-abated value, to any person who is not engaged in a similar business;

   (ii) supply of manpower for any purpose or security services; or

   (iii) service portion in the execution of a works contract;

(hereinafter above mentioned services will be termed as **partial reverse charge services**). The amount of refund would be computed as follows:

Unutilised CENVAT credit taken on inputs and input services during the half year for providing partial reverse charge services → (A)-(B)

where

$$A = \text{CENVAT credit taken on inputs and input services during the half year} \times \frac{\text{Turnover of output service under partial reverse charge duirng the half year}}{\text{Total turnover of goods and services during the half year}}$$

B = Service tax paid by the service provider for such partial reverse charge services during the half year.

(b) Refund shall not exceed the amount of service tax liability paid/payable by the service receiver with respect to the partial reverse charge services provided during the period of half year for which refund is claimed.

(c) Amount claimed as refund shall be debited by the claimant from his CENVAT credit account at the time of making the claim. However, if the amount of refund sanctioned is less than the amount of refund claimed, then the claimant may take back the credit of the difference between the amount claimed and the amount sanctioned.

(d) The claimant shall submit not more than one claim of refund under this notification for every half year.

(e) Refund claim shall be filed after filing of service tax return for the period for which refund is claimed.

(f) No refund shall be admissible for the CENVAT credit taken on input or input services received prior to 01.07.2012.

Half year means a period of six consecutive months with the first half year beginning from the 1st day of April every year and second half year from the 1st day of October of every year.

II. PROCEDURE FOR FILING THE REFUND CLAIM

(a) The output service provider shall submit an application in Form A, along with specified documents and enclosures, to jurisdictional Assistant Commissioner/Deputy Commissioner, before the expiry of 1 year* from the due date of filing of return for the half year. Copies of return(s) filed for the said half year shall also be filed along with the application.

**In case of more than one return required to be filed for the half year, 1 year shall be calculated from due date of filing of the return for the later period.*

However, last date of filing of application in Form A, for the half year ending on 30.09.2012, shall be 30.04.2014.

(b) The Assistant Commissioner/Deputy Commissioner, may call for any document in case he has reason to believe that information provided in the refund claim is incorrect or insufficient and further enquiry needs to be caused before the sanction of refund claim, and shall sanction the claim after satisfying himself that the refund claim is correct and complete in every respect.

2. **Provisions relating to distribution of credit in case of input service distributor amended [Rule 7]**

With effect from 01.04.2014, rule 7 has been amended to simplify the mechanism of distribution of CENVAT credit in case of input service distributor as under:

S. No.	Position as per erstwhile rule 7	Position as per the amended rule 7	
1.	In case of a unit exclusively engaged in manufacture of exempted goods/ providing exempted services, service tax paid on input services **used IN such a unit** was not allowed to be distributed as CENVAT credit.	In case of a unit exclusively engaged in manufacture of exempted goods/ providing exempted services, service tax paid on input services **used BY one or more such units** will not be allowed to be distributed as CENVAT credit	With the substitution of word 'IN' with 'BY', credit of services, which have been used by such units though not actually consumed within such units, would also not be distributed.
2.	Credit of service tax attributable to service **used wholly IN a unit** was to be distributed only to that unit.	Credit of service tax attributable to service **used wholly BY a unit** shall be distributed only to that unit.	Substitution of word 'IN' with 'BY' would increase the scope of services pertaining to which credit could be distributed to a unit. Resultantly, credit for services like good transport agency services, rent-a-cab

			service, testing and analysis of the product etc. would now be available to the unit availing them.
3.	Credit of service tax attributable to service <u>used IN more than one unit</u> was to be distributed pro rata on the basis of the turnover during the relevant period of the concerned unit to the sum total of the turnover of all the units to which the service related during the same period.	Credit of service tax attributable to service <u>used BY more than one unit</u> shall be distributed pro rata on the basis of the turnover of such units during the relevant period to the total turnover of all its units, which are operational in the current year, during the said relevant period.	In case of common input services, amount of CENVAT credit attributed to a unit may be reduced as now turnover of all operational units has to be taken in denominator instead of only the units to which the service relates.
4.	Relevant period was the month/quarter previous to the month/quarter during which the CENVAT credit was distributed. In case of an assessee who did not have any total turnover in the said period, the input service distributor was to distribute any credit only after the end of such relevant period wherein the total turnover of its units was available.	Relevant period shall be the 'financial year' preceding to the year during which credit is to be distributed for month/ quarter provided assessee has turnover in such preceding financial year. If the assessee does not have turnover for some/ all the units in the preceding financial year, relevant period shall be the last quarter for which details of turnover of all the units are available, previous to the month/ quarter for which credit is to be distributed.	Distribution of credit is now based on previous financial year's turnover instead of previous month's/quarter's turnover.

[Notification No. 5/2014-CE (NT) dated 24.02.2014]

3. Amendments in rule 3

(i) Duty leviable on transaction value to be paid on removal of capital goods as waste and scrap [Rule 3(5A)]

Rule 3(5A) of the CENVAT Credit Rules, 2004 provides for reversal of CENVAT credit in the event of removal of capital goods after being used, whether as capital goods or as waste/ scrap. Earlier, the quantum of credit that needs to be reversed was higher of the following two amounts:

(I) CENVAT credit taken on the said capital goods reduced by the specified percentage points calculated by straight line method for each quarter of a year or part thereof from the date of taking the CEVAT credit

or

(II) Duty leviable on transaction value.

However, with effect from 27.09.2013, if the capital goods are cleared as waste and scrap, the manufacturer shall pay an amount equal to the duty leviable on transaction value.

Thus, a manufacturer removing capital goods as waste and scrap will no longer be required to compare the amount equivalent to the duty leviable on transaction value with the amount equivalent to CENVAT credit taken on the said capital goods reduced by the specified percentage points. However, when capital goods will be removed, after being used, otherwise than as waste and scrap, the higher of the above-mentioned two amounts will be required to be paid.

[Notification No. 12/2013 CE (NT) dated 27.09.2013]

(ii) CENVAT credit taken on input services to be reversed if duty paid on final product remitted [Rule 3(5C)]

Earlier, where on any goods manufactured or produced by an assessee, the payment of duty was ordered to be remitted under rule 21 of the Central Excise Rules, 2002, the CENVAT credit taken on the inputs used in the manufacture or production of said goods was required to be reversed. Thus, earlier, reversal was only required in respect of inputs and not for input services.

Rule 3(5C) has been amended to provide that CENVAT credit taken on input services used in or in relation to the manufacture or production of said goods is also required to be reversed.

[Notification No. 1/2014 CE (NT) dated 08.01.2014]

(iii) Amount payable under sub-rules (5), (5A), (5B) and (5C) of rule 3 to be paid on or before the 5th day of the following month by utilizing CENVAT credit or otherwise

As per explanation 1 inserted after rule 3(5C), the amount payable under following sub-rules of rule 3 shall be paid by the manufacturer of goods or the provider of output service

(i)	Rule 3(5)	Reversal of credit in case of removal of inputs or capital goods as such from the factory/premises of the output service provider
(ii)	Rule 3(5A)	Reversal of credit in case of removal of capital goods after being used, whether as capital goods or as scrap or waste
(iii)	Rule 3(5B)	Reversal of credit in case of full or partial writing off of the value of input or capital goods before being put to use
(iv)	Rule 3(5C)	Reversal of credit in case of remission of duty on final product

- by debiting the CENVAT credit or otherwise
- on or before the 5th day of the following month except for the month of March, where such payment shall be made on or before the 31st day of the month of March.

[Notification No. 1/2014 CE (NT) dated 08.01.2014]

(iv) Failure to reverse the credit taken on inputs and input services used in goods on which duty is ordered to be remitted also to attract recovery provisions under rule 14 [Explanation 2 to rule 3(5C)]

Hitherto, as per explanation occurring after proviso to rule 3(5B), recovery provisions under rule 14 of the CENVAT Credit Rules, 2004 were applicable if the manufacturer of goods or the provider of output service fails to pay the amount payable under sub-rules (5), (5A) and (5B) of rule 3.

The said explanation has been omitted and a new explanation 2 has been inserted after rule 3(5C). As per the new explanation 2, in addition to sub-rules (5), (5A) and (5B) of rule 3, recovery provisions under rule 14 will also apply to sub-rule (5C) of rule 3.

In other words, even in a case where the manufacturer of goods or the provider of output service fails to reverse the CENVAT credit taken on inputs and input services used in goods on which duty has been ordered to be remitted, it would be recovered, in the manner provided under rule 14, for recovery of CENVAT credit wrongly taken.

[Notification No. 1/2014 CE (NT) dated 08.01.2014]

4. Importer also required to file quarterly return

Earlier, rule 9(8) required a first stage dealer and a second stage dealer to submit a return (electronically) within 15 days from the close of each quarter of a year to the Superintendent of Central Excise quarterly.

With effect from 01.04.2014, a registered importer is also required to submit such quarterly return.

[Notification No. 9/2014-CE (N.T.) dated 28.02.2014]

SERVICE TAX

I. Exemptions:

1. Mega exemption notification amended

Mega exemption *Notification No. 25/2012-ST dated 30.06.2012* has been amended as follows:-

(a) Services provided by NSDC or by an approved SSC/assessment agency/training partner exempted

Services provided by:-

(i) the National Skill Development Corporation (NSDC) set up by the Government of India;

(ii) a Sector Skill Council (SSC) approved by the NSDC;

(iii) an assessment agency approved by the SSC or the NSDC;

(iv) a training partner approved by the NSDC or the SSC

in relation to:-

(a) the National Skill Development Programme implemented by the NSDC; or

(b) a vocational skill development course under the National Skill Certification and Monetary Reward Scheme; or

(c) any other Scheme implemented by the NSDC

have been exempted from service tax.

[Notification No. 13/2013-ST dated 10.09.2013]

(b) Services provided by cord blood banks by way of preservation of stem cells exempted

Services provided by cord blood banks by way of preservation of stem cells or any other service in relation to such preservation have been exempted from service tax.

[Notification No. 04/2014-ST dated 17.02.2014]

(c) Loading/unloading/packing/storage/warehousing of rice exempted

Services by way of loading, unloading, packing, storage or warehousing of rice have been exempted from service tax.

[Notification No. 04/2014-ST dated 17.02.2014]

(d) Scope of definition of 'Governmental authority' widened

The definition of "Governmental authority" has been substituted with the following new definition:-

"Governmental authority" means an authority or a board or any other body;

(i) set up by an Act of Parliament or a State Legislature; or

(ii) established by Government,

with 90% or more participation by way of equity or control, to carry out any function entrusted to a municipality under article 243W of the Constitution.

Thus, the scope of the definition has been enhanced. Henceforth, an authority or a board or any other body established by Government with 90% or more participation by way of equity or control need not be set up under an Act of Parliament or a State Legislature to qualify as Governmental authority.

[Notification No. 02/2014-ST dated 30.01.2014]

(e) Expansion in the scope of exemption of services provided by way of sponsorship of sports events

Hitherto, services provided by way of sponsorship of sporting events organized by a national sports federation, or its affiliated federations were exempt from service tax where the participating teams or individuals represent any district, State or zone. The said exemption has been extended even in a case where the participating teams or individuals represent any COUNTRY.

[Notification No. 01/2014-ST dated 10.01.2014]

2. Revised scheme of service tax exemption in case of services provided to SEZ unit/Developer

Notification No. 40/2012-ST dated 20.06.2012 prescribing the scheme for claiming exemption in respect of the services received by a developer/units of an SEZ has been superseded by *Notification No. 12/2013-ST dated 01.07.2013.* The new notification has expanded the scope of *ab-initio* exemption and refund available to SEZ unit/developer.

The significant relevant changes in the new notification vis-à-vis erstwhile notification have been outlined as follows:-

Basis	*NN 40/2012*	*NN 12/2013*
Services eligible for *ab initio* exemption	Only specified services wholly consumed within SEZ were eligible for the *ab initio* exemption. Further, the definition of wholly consumed	Specified services received by the SEZ Unit or the Developer used exclusively for the authorized operations are eligible for the *ab initio* exemption.

	services, linked with the Place of Provision of Services Rules, 2012, emphasized that the specified services must be provided only within SEZ.	Consequently, any services used exclusively for the authorized operations whether provided within SEZ or outside, will be eligible for upfront exemption.
Refund of service tax paid on the common services shared between authorized operations in SEZ and its DTA operations	Maximum refund was restricted as under:- Maximum refund $= \frac{ST \times ET}{TT}$ where ST stands for service tax paid on services other than wholly consumed services (used for both SEZ and DTA Unit) ET stands for Export turnover of goods and services of SEZ Unit/Developer TT stands for Total turnover for the period	The service tax paid on the specified services that are common to the authorized operation in an SEZ and the operation in domestic tariff area [DTA unit(s)] shall be distributed amongst the SEZ Unit/Developer and the DTA unit(s) in the manner as prescribed in rule 7 of the CENVAT Credit Rules, 2004. For the purpose of distribution, the turnover of the SEZ Unit/Developer shall be taken as the turnover of authorized operation during the relevant period. Such amount would be available as refund.
Option not to avail the exemption and instead take CENVAT credit as usual	Earlier scheme did not expressly provide for such an option.	SEZ Unit/the Developer has an option not to avail of this exemption and instead take CENVAT credit on the specified services in accordance with the CENVAT Credit Rules, 2004.
Availability of refund of service tax on the specified services on which *ab-initio* exemption is admissible but not claimed	Refund of service tax on the specified services on which *ab-initio* exemption is admissible but not claimed was not expressly provided in the earlier scheme.	The SEZ Unit or the Developer shall be entitled to the refund of service tax on the specified services on which *ab-initio* exemption is admissible but not claimed.

II. Threshold limit for e-payment of service tax reduced from ₹ 10 lakh to ₹ 1 lakh

Proviso to rule 6(2) of the Service Tax Rules, 1994 has been amended to reduce the threshold limit for e-payment of service tax from ₹ 10 lakh to ₹ 1 lakh. Henceforth, with effect from 01.01.2014, where an assessee has paid a total service tax of ₹ 1 lakh or more including the amount paid by utilization of CENVAT credit, in the preceding financial year, he shall deposit the service tax liable to be paid by him electronically through internet banking.

[Notification No. 16/2013-ST dated 22.11.2013]

III. Clarifications

1. Clarification as to whether "agricultural produce" includes rice and benefits available in respect of rice under mega exemption notification

CBEC vide *Circular No.177/03/2014 – ST dated 17.02.2014,* has clarified that the definition of agricultural produce under section 65(5) of the Finance Act, 1994 covers 'paddy'; but excludes 'rice'. It implies that benefits available to agricultural produce in the negative list [Section 66D(d)] are not available to rice.

However, many such benefits have been extended to rice by way of appropriate entries in the mega exemption notification as follows:-

(i) Services by way of transportation of food stuff by rail/vessel/goods transport agency is exempt from service tax. Food stuff includes rice.

(ii) Services by way of loading, unloading, packing, storage or warehousing of rice are exempt from service tax.

(iii) Carrying out an intermediate production process as job work in relation to agriculture is exempt from service tax. It is clarified that paddy milled into rice, on job work basis is also exempt from service tax since such milling of paddy is an intermediate production process in relation to agriculture.

2. Clarification regarding exemption available to services provided by a Resident Welfare Association (RWA) to its own members

Mega exemption *Notification No. 25/2012-ST dated 20.06.2012* provides exemption to services provided by an RWA to its own members by way of reimbursement of charges or share of contribution up to ₹ 5,000 per month per member for sourcing of goods or services from a third person for the common use of its members.

Certain doubts have been raised regarding the scope of said exemption. CBEC vide *Circular No.175/01/2014 – ST dated 10.01.2014*, has clarified these doubts as follows:

Sl. No.	Doubt	Clarification
1.	(i) In a residential complex, monthly contribution collected from members is used by the RWA for the purpose of making payments to the third parties, in respect of commonly used services or goods	Exemption in mega exemption notification is provided specifically with reference to service provided by an unincorporated body or a non–profit entity registered under any law for the time being in force such as RWAs, to its own members.

	[Example: for providing security service for the residential complex, maintenance or upkeep of common area and common facilities like lift, water sump, health and fitness centre, swimming pool, payment of electricity Bill for the common area and lift, etc.]. Is service tax leviable on the same? (ii) If the contribution of a member(s) of a RWA exceeds ₹ 5,000 per month, how should the service tax liability be calculated?	However, a monetary ceiling has been prescribed for this exemption, calculated in the form of ₹ 5,000 per month per member contribution to the RWA, for sourcing of goods or services from third person for the common use of its members. If per month per member contribution of any or some members of a RWA exceeds ₹ 5,000, entire contribution of such members whose per month contribution exceeds ₹ 5,000 would be ineligible for the exemption under the said notification. Service tax would then be leviable on the aggregate amount of monthly contribution of such members.
2.	(i) Is Small Service Provider's (SSP) exemption under *Notification No. 33/2012-ST* available to RWA? (ii) Does 'aggregate value' for the purpose of threshold exemption, include the value of exempt service?	SSP exemption under *Notification No. 33/2012-ST* is applicable to a RWA, subject to conditions prescribed in the notification. Under this notification, taxable services of aggregate value not exceeding ₹ 10 lakh in any financial year is exempted from service tax. As per the definition of 'aggregate value' provided in explanation of the notification, aggregate value does not include the value of services which are exempt from service tax.
3.	If a RWA provides certain services such as payment of electricity or water bill issued by third person, in the name of its members, acting as a 'pure agent' of its members, is exclusion from value of taxable service available for the purposes of SSP exemption or exemption provided under mega exemption notification?	In Rule 5(2) of the Service Tax (Determination of Value) Rules, 2006, it is provided that expenditure or costs incurred by a service provider as a pure agent of the recipient of service shall be excluded from the value of taxable service, subject to the conditions specified in the said rule. For example, where the payment for an electricity bill raised by an electricity transmission or distribution utility in the name of the owner of an apartment in respect of electricity consumed thereon, is collected and paid by the RWA to the

		utility, without charging any commission or a consideration by any other name, the RWA is acting as a pure agent and hence exclusion from the value of taxable service would be available. However, in the case of electricity bills issued in the name of RWA, in respect of electricity consumed for common use of lifts, motor pumps for water supply, lights in common area, etc., since there is no agent involved in these transactions, the exclusion from the value of taxable service would not be available.
4.	Is CENVAT credit available to RWA for payment of service tax?	RWA may avail CENVAT credit and use the same for payment of service tax, in accordance with the CENVAT Credit Rules, 2004.

PART – II: QUESTIONS AND ANSWERS

QUESTIONS

Residential Status and Scope of total income

1. From the following particulars of income furnished by Mr. Anand pertaining to the year ended 31.3.2014, compute his total income for the assessment year 2014-15, if he is:

   (i) Resident and ordinarily resident;

   (ii) Resident but not ordinarily resident;

   (iii) Non-resident

	Particulars	₹
(a)	Short term capital gain on sale of shares in Indian Company received in Japan	25,000
(b)	Dividend from a South African company received in South Africa	20,000
(c)	Rent from property in UK deposited in a bank in UK, later on remitted to India through approved banking channels	1,50,000
(d)	Dividend from SK Ltd., an Indian Company	12,000
(e)	Agricultural income from land in Madhya Pradesh	56,000

Income which do not form part of total income

2. (i) A special purpose distinct entity (regulated by SEBI), set up in the form of a trust to undertake securitization activities, receives ₹ 20 lakh from the activities of

securitisation and distributes ₹ 5 lakh to its investors. What would be the tax implications in the hands of :-

(a) the special purpose distinct entity, in respect of its income from the activity of securitisation; and

(b) investors, in respect of income distributed by the special purpose distinct entity.

(ii) Discuss the taxability or otherwise of the income of Investor Protection Fund (IPF), by way of contributions received from;

(a) a recognised stock exchange and its members, where the IPF is set up by the recognised stock exchange.

(b) a depository, where the IPF is set up by the depository.

(iii) Determine the taxability of the following sums received by Mr. Tularam from LIC on account of the life insurance policies taken by him -

S. No.	Date of Issue of policy	Person insured	Actual capital sum Assured	Annual Insurance Premium	Sums received as bonus during the previous year 2013-14
1.	20.10.2010	Minor Son	5,00,000	75,000	60,000
2.	10.06.2012	Spouse	2,00,000	30,000	15,000
3.	11.04.2013	Handicapped daughter (section 80U disability)	8,00,000	1,00,000	18,000

Income from Salaries

3. (a) Mrs. Meera, aged about 65 years, is the HR Manager of M/s. Alpha Pvt. Ltd., based at Mumbai. She is in continuous service since 1980 and receives the following salary and perks from the company during the year ending 31.03.2014:

(i) Basic Salary (₹ 60,000 x 12) = ₹ 7,20,000

(ii) D.A. (₹ 24,000 x 12) = ₹ 2,88,000 (forms part of pay for retirement benefits)

(iii) Bonus – 1.5 months basic salary.

(iv) Commission – 0.1% of the turnover of the company. The turnover for the F.Y. 2013-14 was ₹ 50.00 crores.

(v) Contribution of the employer and employee to the recognized provident fund Account ₹ 3,50,000 each.

(vi) Interest credited to Recognized Provident Fund Account at 9.5% - ₹ 80,000.

(vii) Rent free unfurnished accommodation provided by the company for which the company pays a rent of ₹ 1,00,000 per annum.

(viii) Entertainment Allowance – ₹ 25,000.

(ix) Hostel allowance for three children – ₹ 3,500 each.

She makes the following payments and investments:

(i) Premium paid to insure the life of her major son – ₹ 20,000. Actual Capital Sum Assured is ₹ 2,00,000

(ii) Medical Insurance premium for self & spouse ₹ 18,000.

(iii) Donation of ₹ 1,50,000 to approved public charitable institution by way of cheque.

(iv) LIC Pension Fund – ₹ 15,000.

Determine the tax liability for the Assessment Year 2014-15.

(b) Mr. Arpan, a Government employee, retired on 28-02-2014 after rendering service of 27 years and 8 months. He received gratuity of ₹ 12,00,000. His salary at the time of retirement was as under:

Basic salary ₹ 38,000 p.m.

Dearness Allowance ₹ 25,000 p.m.

(i) Compute the taxable gratuity.

(ii) If Mr. Arpan is not a Government employee but covered by Payment of Gratuity Act, 1972, what would be the taxable gratuity?

(iii) Would your answer be different if he was not covered by Payment of Gratuity Act, 1972?

Income from house property

4. Mr. Karan and Mr. Kunal constructed their houses on a piece of land purchased by them at Kanpur. The built up area of each house was 1,250 sq.ft. ground floor and an equal area in the first floor. Karan started construction on 1-04-2012 and completed on 1-04-2013. Kunal started the construction on 1-07-2012 and completed the construction on 30-06-2013. Karan occupied the entire house on 01-04-2013. Kunal occupied the ground floor on 01-07-2013 and let out the first floor for a rent of ₹ 25,000 per month. However, the tenant vacated the house on 30-11-2013 and Kunal occupied the entire house during the period 01-12-2013 to 31-03-2014.

Following are the other information:

(i)	Fair rental value of each unit (ground floor/first floor)	₹ 1,25,000 per annum
(ii)	Municipal value of each unit (ground floor/first floor)	₹ 80,000 per annum
(iii)	Municipal taxes paid by	Karan – ₹ 10,000

		Kunal – ₹ 10,000
(iv)	Repair and maintenance charges paid by	Karan – ₹ 35,000
		Kunal– ₹ 32,000

Karan has availed a housing loan of ₹ 30 lakh @ 11% p.a. on 01-04-2012. Kunal has availed a housing loan of ₹ 25 lakh @ 10% p.a. on 01-07-2012. No repayment was made by either of them till 31-03-2014. Compute income from house property for Karan and Kunal for the A.Y. 2014-15.

Profits and gains of business or profession

5. (a) M/s. Amla Ltd., a manufacturing concern, furnishes the following particulars for the P.Y. 2013-14:

		₹ (in crore)
(i)	Opening written down value of plant and machinery (15% block)	50.00
(ii)	Purchase of plant and machinery (put to use on 10.09.2013)	106.00
(iii)	Sale proceeds of plant and machinery which became obsolete- the plant and machinery was purchased on 01-04-2011 for ₹ 0.50 crore.	0.20

Further, out of purchase of plant and machinery:

(a) Plant and machinery of ₹ 0.30 crore has been installed in office.

(b) Plant and machinery of ₹ 0.20 crore was used previously for the purpose of business by the seller.

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

(b) Mr. Jagat engaged in retail trade, reports a turnover of ₹ 82,46,000 for the financial year 2013-14. His income from the said business as per books of account is computed at ₹ 5,85,600. Retail trade is the only source of income for Mr.Jagat.

(i) Is Mr. Jagat eligible to opt for presumptive taxation of his income chargeable to tax for the assessment year 2014-15?

(ii) If so, determine his income from retail trade as per the applicable presumptive provision.

(iii) In case Mr. Jagat does not opt for presumptive taxation of income from retail trade, what are his obligations under the Income-tax Act, 1961?

(iv) What is the due date for filing his return of income under both the options?

Capital Gains

6. Ms. Gunjan purchased a land at a cost of ₹ 50 lakh in the financial year 2000-01 and held the same as her capital asset till 31st August, 2012. She started her real estate business on 1st September, 2012 and converted the said land into stock-in-trade of her business on the said date, when the fair market value of the land was ₹ 320 lakh.

   She constructed 8 flats of equal size, quality and dimension. Cost of construction of each flat is ₹ 36 lakh. Construction was completed in January, 2014. She sold 5 flats at ₹ 90 lakh per flat in February, 2014.

   She invested ₹ 70 lakh in bonds issued by National Highways Authority of India on 31st March, 2014.

   Compute the capital gains and business income arising from the above transactions in the hands of Ms. Gunjan for Assessment Year 2014-15 indicating clearly the reasons for treatment for each item.

   Cost Inflation Indices: F.Y. 2000-01: 406; F.Y.2012-13: 852; F.Y. 2013-14: 939.

Income from Other Sources

7. Discuss the tax implications under section 56(2) in respect of each of the following transactions -

   (i) Mr. Tejpal received a painting by M. F. Hussain worth ₹ 2 lakh from his nephew on his 10th wedding anniversary.

   (ii) Verma's son transferred shares of D Ltd. to Verma HUF without any consideration. The fair market value of the shares is ₹ 2.5 lakh.

   (iii) Sunshine (P) Ltd. purchased 9,500 equity shares of Saturn (P) Ltd. at ₹ 86 per share. The fair market value of the share on the date of transaction is ₹ 105.

   (iv) Bijali (P) Ltd. issued 28,000 equity shares of ₹ 10 each at a premium of ₹ 8. The fair market value of each share on the date of issue is ₹ 15.

   (v) Mr. Sharan's land was acquired by the Government in August 2010. He received interest of ₹ 5,40,000 on enhanced compensation in January, 2014, out of which ₹ 1,20,000 related to the year 2010-11, ₹ 1,60,000 related to the year 2011-12, ₹ 2,00,000 related to the year 2012-13 and 60,000 related to the year 2013-14.

Profits and gains of business or profession, Capital Gains & Income from Other Sources

8. Mr. Suraj, a Sales Manager with Moon Ltd., sold a building to his friend Mr. Rohan, who is engaged in the business of artificial jewellery, for ₹ 80 lakh on 01.01.2014, when the stamp duty value was ₹ 220 lakh. The agreement was, however, entered into on 04.06.2013 when the stamp duty value was ₹ 150 lakh. Mr. Suraj had received a down payment of ₹ 30 lakh by cheque from Mr. Rohan on the date of agreement. Discuss the tax implications in the hands of Mr. Suraj and Mr. Rohan, assuming that Mr. Suraj had purchased the building for ₹ 61 lakh on 20th October, 2011.

Would your answer be different if Mr. Suraj was a property dealer and he sold the building to Mr. Rohan in the course of his business?

Income of Other Persons included in assessee's Total Income

9. A proprietary business was started by Smt. Reena in the year 2011. As on 1.4.2012, her capital in business was ₹ 5,00,000.

   Her husband gifted ₹ 3,50,000 on 15.05.2012, which was invested in her business on the same date. Smt. Reena earned profits from her proprietary business for the Financial year 2012-13, ₹ 2,00,000 and Financial year 2013-14 ₹ 5,10,000. Compute the income, to be clubbed in the hands of Reena's husband for the Assessment year 2014-15 with reasons.

Set off and Carry Forward of Losses

10. The following are the details relating to Mr. Sitaraman, a resident Indian, aged 57, relating to the year ended 31.3.2014:

Particulars	₹
Income from salaries	3,22,000
Loss from house property	1,65,000
Loss from retail business	2,25,000
Income from speculation business	26,000
Loss from specified business covered by section 35AD	31,000
Long-term capital gains from sale of residential house	3,60,000
Long-term capital loss from sale of listed shares in recognized stock exchange (STT paid)	1,21,000
Loss from card games	33,000
Income from betting (Gross)	51,000
Life Insurance Premium paid (policy taken on 10^{th} August 2012 for actual capital sum assured of ₹ 9 lakh)	1,00,000

Compute the total income and show the items eligible for carry forward.

Deductions from Gross Total Income

11. Mr. Rakesh, Mr. Jaiprakash and Mr. Himesh, new retail investors, have made the following investments in equity shares/units of equity oriented fund of Rajiv Gandhi Equity Savings Scheme for the P.Y.2013-14 as below :

	Particulars	Mr. Rakesh	Mr. Jaiprakash	Mr. Himesh
		₹	₹	₹
(i)	Investment in listed equity shares	35,000	35,000	28,000

(ii)	Investment in units of equity-oriented fund	25,000	-	15,000
(iii)	Gross Total Income (comprising of salary income and bank interest)	9,26,000	12,81,000	10,17,000

Compute the deduction available to Mr. Rakesh, Mr. Jaiprakash & Mr. Himesh under section 80CCG for the A.Y. 2014-15.

What would be the tax consequences if Mr. Jaiprakash & Mr. Himesh sold the entire investment made in listed equity shares in January 2015?

Computation of Total Income of an individual

12. Dr. Sonia, a resident individual, aged 60 years is running a clinic. Her Income and Expenditure Account for the year ending March 31st, 2014 is as under:

Expenditure	₹	Income	₹
To Medicine consumed	6,72,340	By Consultation and Medical charges	19,96,750
To Staff salary	4,20,000	By Income-tax refund (Principal ₹ 4,800, interest ₹ 650)	5,450
To Clinic consumables	1,42,000	By Dividend from units of UTI	9,400
To Rent paid	75,000	By winning from game show on T.V. (net of TDS of ₹ 15,600)	36,400
To Administrative expenses	2,81,000	By Rent	36,000
To Amount paid to scientific research association approved under section 35	1,80,000		
To Net profit	3,13,660		
	20,84,000		20,84,000

(i) Rent paid includes ₹ 37,000 paid by cheque towards rent for her residential house in Gwalior.

(ii) Clinic equipments are:

01.04.2013 Opening W.D.V. - ₹ 4,50,000

15.01.2014 Acquired (cost) - ₹ 2,25,000

(iii) Rent received relates to property situated at Gwalior. Gross Annual Value ₹ 36,000. The municipal tax of ₹ 2,800, paid in January, 2014, has been included in "administrative expenses".

(iv) She received salary of ₹ 15,000 p.m. from "Radha Krishnan Hospital" which has not been included in the "consultation and medical charges".

(v) Dr. Sonia availed a loan of ₹ 7,50,000 from a bank for higher education of her daughter. She repaid principal of ₹ 80,000, and interest thereon ₹ 75,000 during the year 2013-14.

(vi) She paid ₹ 80,000 as tuition fee (not in the nature of development fees/ donation) to the university for full time education of her daughter.

(vii) An amount of ₹ 23,000 has also been paid by cheque on 15th February, 2014 for her medical insurance premium.

From the above, compute the total income of Dr. Sonia for the A.Y. 2014-15.

Provisions concerning deduction of tax at source/Provisions for filing of Return of Income

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

(i) Mr. Jagdish sold his house property in Delhi as well as rural agricultural land for a consideration of ₹ 80 lakh and ₹ 25 lakh, respectively, to Mr. Siddharth on 31st August 2013.

(ii) Payment of royalty of ₹ 25,000 and fee for professional services of ₹ 28,000 to Mr. Varun.

(iii) Punjab National Bank pays ₹ 1,00,000 per month as rent to the Central Government for a building in which one of its branches is situated.

(iv) Payment of ₹ 1,98,000 on 01.05.2013 to Mr. Karan for compulsory acquisition of his urban land by the State Government.

(b) Mr. Rajveer is a resident Indian. During the F.Y. 2013-14, interest of ₹ 3,06,000 was credited to his Non-resident (External) Account with the SBI. ₹ 25,000 being interest on fixed deposit with SBI was credited to his savings bank account during this period. He also earned ₹ 9,600 as interest on this savings account. Is Mr. Rajveer required to file return of income?

What will be your answer, if he owns a house in London?

Exemption from service tax

14. X Techies Ltd. imported a taxable service (involving transfer of technology) for ₹ 12,00,000 from USA in the month of June, 2013. The exporter raised an invoice for the same on 01.07.2013. X Techies Ltd. paid the said amount on 10.12.2013. The

Research and Development cess (R & D cess) of ₹ 60,000 leviable on such import of technology was paid by X Techies Ltd. on 22.11.2013. You are required to answer the following with respect to the given transaction:

(i) Who is liable to pay service tax?

(ii) What is the point of taxation?

(ii) What is the amount of service tax payable on the said taxable service?

Note:

(1) X Techies Ltd. has maintained proper records which show the linkage between the invoice raised for the service and R&D cess payment challan.

(2) ₹ 12,00,000 is exclusive of service tax and R & D cess.

Basic concepts of service tax

15. BTR Association, an unincorporated body of individuals, provided warehousing services to Mr. Raman for ₹ 15,00,000. BTR Association is of the view that since it is not a natural person, warehousing service provided by it will not be a *'service'* in terms of section 65B(44) of the Finance Act, 1994.

    Examine whether the view taken by BTR Association is valid in law.

Computation of service tax

16. Ms. Kohana has provided you the following details in respect of various services received/availed by her during December, 2013:-

    (i) Deposited ₹ 1,00,000 in her Savings Bank A/c. Interest of ₹ 5,000 was credited in her account on 31.12.2013.

    (ii) Availed services of a mobile network operator and received a monthly bill for ₹ 2,000.

    (iii) Visited an Orthopaedician (MBBS, MS) as she had severe backache and paid consultancy fee of ₹ 1,000.

    (iv) Availed beauty treatment services from a salon for ₹ 6,000.

    Notes:

    1. All the amounts given above, are exclusive of service tax, wherever applicable.
    2. All the service providers who have provided services to Ms. Kohana are not eligible for small service provider's exemption, wherever service tax is applicable.
    3. Wherever applicable, service tax is to be recovered from the service receiver.

    Compute the amount of service tax leviable on services availed/received by Ms. Kohana.

Point of taxation

17. Sunidhi & Co. provided business support services to Bansi on 10th March, 2014 for ₹ 50,000. The invoice for the same was issued on 20th March, 2014. Sunidhi & Co. received the payment against the said invoice on 15th March, 2014 vide cheque dated 12th March, 2014. The entry for the receipt of payment was made in the books of accounts on 15th March, 2014 itself. However, the amount was credited in the bank A/c on 25th March, 2014.

    Determine the point of taxation in the given case.

Valuation of taxable service

18. Well-Being Nursing Home has received the following amounts in the month of February, 2014 in lieu of various services rendered by it in the same month. You are required to determine its service tax liability for February, 2014 from the details furnished below:-

S. No.	Particulars	(₹) (in lakh)
(i)	Palliative care for terminally ill patients at patient's home *(Palliative care is given to improve the quality of life of patients who have a serious or life-threatening disease but the goal of such care is not to cure the disease)*	30
(ii)	Services provided by cord blood bank unit of the nursing home by way of preservation of stem cells	24
(iii)	Hair transplant services	100
(iv)	Ambulance services to transport critically ill patients from various locations to nursing home	12
(v)	Naturopathy treatments. *Such treatment is a recognized system of medicine in terms of section 2(h) of the Clinical Establishments Act, 2010*	80
(vi)	Plastic surgery to restore anatomy of a child affected due to an accident.	30
(vii)	Pranic healing treatments. *Such treatment is not a recognized system of medicine in terms of section 2(h) of the Clinical Establishments Act, 2010*	120
(viii)	Mortuary services	10

Note: All the amounts given above are exclusive of service tax. Further, Well-Being Nursing Home is not eligible for the small service provider's exemption under Notification No. 33/2012-ST dated 20.06.2012. Point of taxation for the services rendered by Well-Being Nursing Home in the month of February, 2014 fall in the month of February itself.

Basic concepts of service tax

19. Shyam has given his tempos on hire to Mohan Brothers for transportation of food stuff for ₹ 40,00,000. He has also transferred the right to use such tempos to Mohan Brothers. Shyam has not paid any service tax on the consideration so received. Discuss whether Shyam is liable to pay service tax on the said transaction.

CENVAT credit

20. LMN (Pvt.) Ltd. is engaged in providing taxable services to its clients. Its service tax liability for the month of January, 2014 is ₹ 3,50,000. LMN (Pvt.) Ltd. intends to make e-payment of service tax on the due date i.e., on 06.02.2014.

    Break-up of CENVAT credit available with LMN Ltd. as on 01.01.2014 is given below:

Particulars	*(₹)*
Inputs	50,000
Capital goods	1,00,000
Input services	15,000

LMN (Pvt.) Ltd. has provided the following further details:

Particulars	Excise duty		Service tax (₹) [Input services]
	Inputs (₹)	Capital goods (₹)	
Inputs received on 10.01.2014	30,000		
Inputs received on 15.01.2014	50,000		
Capital goods received on 20.01.2014		70,000	
Invoices (for input services) dated 23.01.2014 received on same day			35,000
Invoices (for input services) dated 02.02.2014 received on same day			35,000
Inputs received on 04.02.2014	45,000		

Out of total duty of ₹ 50,000 paid on inputs received on 15.01.2014, ₹ 15,000 represented National Calamity Contingent Duty.

You are required to determine the service tax payable by LMN (Pvt.) Ltd. in cash, if any. [Ignore EC and SHEC.]

Note: LMN (Pvt.) Ltd. is not eligible for the small service provider exemption under *Notification No. 33/2012-ST dated 20.06.2012*.

Computation of central excise duty and customs duty payable

21. (a) Grand India Ltd. sold a machine, manufactured by it, to Indian Industries Ltd. (IIL) at

a price of ₹ 10,00,000 (excluding taxes and duties). Further, following additional amounts were also charged:

Particulars	(₹)
Expenses pertaining to installation and erection of the machine at premises of IIL (machine was permanently affixed to earth)	30,000
Special packing charges	12,500
Design and engineering charges	40,000
Dharmada (charged in the invoice and recovered from IIL)	10,000

Determine the total amount of central excise duty payable on the machine from the aforesaid information.

(b) Sneha Subramanian imports a carton of goods from Germany on 10.01.2014 containing 8,000 pieces with assessable value of ₹ 1,20,000 under section 14 of the Customs Act, 1962. On the said product, rate of basic customs duty is 10% and rate of excise duty is 12% ad valorem. Similar product in India is assessable under section 4A of the Central Excise Act, 1944, after allowing an abatement of 30%. MRP printed on the package at the time of import is ₹ 30 per piece.

Calculate the countervailing duty (CVD) under section 3(1) of the Customs Tariff Act, 1975 payable on the imported goods.

Computation of net VAT liability

22. Compute net VAT payable by Rainbow & Co. from the following details furnished by it for the month of March, 2014:-

Inputs procured		(₹)
(i)	Raw material at Nil rate of VAT	5,00,000
(ii)	Raw material at 4% VAT	20,00,000
(iii)	Raw material at 12% VAT	10,00,000
Output		**(₹)**
(i)	Intra-State sale of finished goods at 4% VAT (these goods were produced entirely from raw material procured at Nil VAT)	8,00,000
(ii)	Exempted sales (60% of the raw material procured at 4% VAT was used in producing these goods)	10,00,000
(iii)	Intra-State sale of finished goods at 12% VAT	10,00,000
(iv)	Intra-State sale of raw material purchased at 4% VAT	5,00,000
(v)	50% of the raw material produced at 12% VAT has been utilised to produce capital goods for the manufacturing process in Rainbow & Co's factory (Market Value is ₹ 7,50,000)	

There was no opening and closing stock of goods.

Determination of turnover for central sales tax

23. Mediatek Pvt. Ltd.'s total inter-State sales @ 4% CST for the Financial Year 2013-14 is ₹ 2,00,00,000 (CST not shown separately). In this regard, following additional information is available:

(i) Goods sold to Amit for ₹ 1,50,000, on 10.07.2013 were returned by him on 08.12.2013.

(ii) A buyer, Sumit, to whom goods worth ₹ 45,000 were dispatched on 25.08.2013, rejected such goods. The said goods were received back on 10.03.2014.

(iii) Goods sold to Shyam for ₹ 3,00,000, on 11.07.2013 were returned by him on 12.02.2014.

Determine the amount of taxable turnover of Mediatek Pvt. Ltd.

SUGGESTED ANSWERS/HINTS

1. **Computation of total income of Mr. Anand for A.Y. 2014-15**

Particulars	Resident & ordinarily resident	Resident but not ordinarily resident	Non-Resident
1) Short term capital gain on sale of shares in an Indian company, received in Japan	25,000	25,000	25,000
2) Dividend from a South African company, received in South Africa	20,000	-	-
3) Rent from property in UK deposited in a bank in UK [See Note (ii) below]	1,05,000	-	-
4) Dividend from SK Ltd., an Indian Company [See Note (iii) below]	-	-	-
5) Agricultural income from land in Madhya Pradesh [See Note (iv) below]	-	-	-
Total Income	1,50,000	25,000	25,000

Notes:

(i) Global income is taxable in case of a resident & ordinarily resident as per section 5(1). In case of a not ordinarily resident, income which accrues or arises outside India would be taxable only if it is from a business controlled from or profession set up in India. As per section 5(2), in case of a non-resident, only the following incomes are taxable –

(a) Income which accrues or arises or is deemed to accrue or arise in India.

(b) Income received or deemed to be received in India.

Accordingly, dividend from a South African company and rent from property in UK is taxable only in case of resident & ordinarily resident. However, short term capital gain on sale of shares in an Indian company is taxable in all three cases, since it accrues or arises in India.

(ii) It has been assumed that the rental income is the gross annual value of the property. Therefore, deduction @30% under section 24, has been provided and the net income so computed is taken into account for determining the total income of a resident and ordinarily resident.

Rent received (assumed as gross annual value)	1,50,000
Less: Deduction under section 24 (30% of ₹ 1,50,000)	45,000
Income from house property	1,05,000

(iii) Dividend from Indian company is exempt under section 10(34).

(iv) Agricultural income from land situated in India is exempt under section 10(1).

2. (i) (a) As per section 10(23DA), in case of special purpose distinct entities set up as a trust and whose activities are regulated by SEBI, the income from the activity of securitization of such trusts will be exempt from taxation.

In this case, since income of ₹ 20 lakh arises to the special purpose distinct entity, set up as a trust, from the activity of securitization, the same would be exempt under section 10(23DA).

(b) As per section 10(35A), the distributed income received from a securitization trust will be exempt from tax in the hands of recipient investors.[1]

(ii) In case of an Investor Protection Fund set up by a recognized stock exchange in India, section 10(23EA) exempts income by way of contributions received by such Investor Protection Fund from the recognized stock exchange and its members thereof.

As per section 10(23ED), the income by way of contributions from depository of an Investor Protection Fund set up in accordance with the regulations made under the SEBI Act, 1992 and the Depositories Act, 1996 will not be included while computing the total income of such Investor Protection Fund.

[1] The distributed income is exempted in the hands of recipient investor consequent to the levy of additional income tax under section 115TA on such distributed income in the hands of securitization trust.

(iii) Taxability of the sums received by way of bonus in the hands of Mr. Tularam from LIC shall be determined in accordance with the provisions of section 10(10D) in the following manner:

S. No.	Date of Issue of policy	Person insured	Actual capital sum Assured	Annual Insurance Premium	Sums received as bonus during the previous year 2013-14
1.	20.10.2010	Minor Son	5,00,000	75,000	60,000
	Taxability: Sum received is exempt under section 10(10D), as the policy is issued on or before 31.3.2012 and the annual premium does not exceed 20% of the Actual Capital Sum Assured.				
2.	10.06.2012	Spouse	2,00,000	30,000	15,000
	Taxability: Sum received is taxable, as the policy is issued after 1.4.2012 and the annual premium exceeds 10% of the Actual Capital Sum Assured.				
3.	11.04.2013	Handicapped daughter (section 80U disability)	8,00,000	1,00,000	18,000
	Taxability: Sum received is exempt under section 10(10D), since the policy is issued after 1.4.2013 for insuring the life of the handicapped daughter, being a person with section 80U disability, and the annual premium does not exceed 15% of the Actual Capital Sum Assured.				

3 (a) **Computation of total income and tax liability of Mrs. Meera for A.Y. 2014-15**

Particulars	₹	₹
Income from salary		
Basic salary		7,20,000
Dearness allowance		2,88,000
Bonus (₹ 60,000 x 1.5 months)		90,000
Commission (calculated as percentage of turnover)[0.1% of ₹ 50 crore)		5,00,000
Entertainment allowance		25,000

Children's hostel allowance (₹ 3,500 x3)	10,500	
Less : Exemption for ₹ 7,200 (₹ 300 x 12 x 2), but restricted to actual amount received for 2 children i.e. ₹ 7,000 (3500 x 2)	7,000	3,500
Interest credited to recognized provident fund account (exempt)		-
Rent free unfurnished accommodation (Refer Working Note 1)		1,00,000
Excess contribution to PF by employer (Refer Working Note 2)		1,69,040
Gross salary		18,95,540
Less : Deduction under section chapter VI-A		
Deduction under section 80C		
• Life insurance premium paid for insurance of major son, allowed as deduction since it is within the limit of 10% of ₹ 2,00,000 (actual capital sum assured)	20,000	
• Contribution to recognized provident fund	3,50,000	
Deduction under section 80CCC (LIC pension fund)	15,000	
	3,85,000	
Deduction limited to ₹ 1,00,000 as per section 80CCE		1,00,000
Deduction under section 80D (Medical Insurance premium for self and spouse)		18,000
Total income before deduction under section 80G		17,77,540
Deduction under section 80G :		
50% of ₹ 1,50,000 (Refer Working Note 3)		75,000
Total income		17,02,540
Tax on total income		3,35,762
Add : Education cess @ 2%		6,715
Add : Secondary and higher education cess @ 1%		3,358
Total tax liability		3,45,835
Total tax liability (Rounded off)		3,45,840

Working Notes:

1 Value of rent free unfurnished accommodation

Particulars	₹
Basic salary	7,20,000
Dearness allowance	2,88,000
Bonus	90,000
Commission @ 0.1% of turnover	5,00,000
Entertainment allowance	25,000
Children's hostel allowance	3,500
Gross Salary	16,26,500
Value of perquisite:	
(i) 15% of salary	2,43,975
(ii) Actual rent paid by the company	1,00,000
The lower of (i) and (ii) is chargeable as perquisite.	

2. Employer's contribution to P.F. in excess of 12% of salary

Employer's contribution	₹ 3,50,000
Less : 12% of basic salary, dearness allowance & commission i.e. 12% of ₹ 15,08,000	₹ 1,80,960
	₹ 1,69,040

3. Donation to approved Public Charitable Institution by way of cheque qualifies for deduction under section 80G.

   Net qualifying amount is lower of:-

   (i) ₹ 1,50,000 (the amount of donation); or

   (ii) ₹ 1,77,754 (10% of adjusted gross total income i.e. 10% of ₹ 17,77,540)

   Therefore, ₹ 75,000 (50% of ₹ 1,50,000) is allowed as deduction under section 80G.

(b) (i) As per section 10(10)(i), gratuity received by a Government employee on retirement is fully exempt from tax. Since Mr. Arpan is a government employee, gratuity amounting to ₹ 12,00,000 received would be fully exempt. The taxable portion of gratuity shall be Nil.

(ii) If Mr. Arpan is not a Government employee but covered by the Payment of Gratuity Act, 1972, then, gratuity received by him would be exempt upto least of the following :

Particulars		₹
(i)	Statutory limit	10,00,000
(ii)	Actual gratuity received	12,00,000
(iii)	15/26 x last drawn salary x years of service (including part of the year in excess of 6 months) 15/26 x ₹ 63,000 x 28 years	10,17,692

Therefore, ₹ 10,00,000 is exempt under section 10(10)(ii).

Taxable gratuity = ₹ 12,00,000 – ₹ 10,00,000 = ₹ 2,00,000

Salary, for the purpose of computing exempt gratuity in this case, means basic salary plus dearness allowance i.e. ₹ 63,000 (₹ 38,000 + ₹ 25,000).

(iii) If Mr. Arpan is not a Government employee and not covered under the Payment of Gratuity Act, 1972 then, gratuity received by him would be exempt upto the least of the following:

Particulars		₹
(i)	Statutory limit	10,00,000
(ii)	Actual gratuity received	12,00,000
(iii)	1/2 x Average salary of 10 months immediately preceding the month of retirement x years of service (shall not include part of the year in excess of 6 months)1/2 x ₹ 38,000 x 27 years	5,13,000

Therefore, ₹ 5,13,000 is exempt under section 10(10)(iii) The taxable gratuity is ₹ 6,87,000 (₹ 12,00,000 – ₹ 5,13,000)

Salary, for the purpose of computation of exempt gratuity, means basic salary of ₹ 38,000 p.m [Average salary for 10 months = (₹ 38,000x10)/10]

Note: It is assumed that dearness allowance does not form part of salary for retirement benefits.

4. **Computation of income from house property of Mr. Karan for A.Y. 2014-15**

Particulars	₹	₹
Annual Value is nil (since house is self occupied)		Nil
Less : Deduction under section 24(b)		
Interest paid on borrowed capital ₹ 30,00,000 @ 11%	3,30,000	
Pre-construction interest ₹ 3,30,000 / 5	66,000	
	3,96,000	
As per second proviso to section 24(b), interest deduction restricted to		1,50,000
Loss under the head "income from house property" of Mr. Karan		(1,50,000)

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

Particulars	Ground floor (Self occupied)	First floor
Gross Annual Value (See Note below)	Nil	1,25,000
Less :Municipal taxes (for first floor)	____	5,000
Net Annual Value (A)	Nil	1,20,000
Less : Deductions under section 24		
(a) 30% of Net Annual Value		36,000
(b) Interest on borrowed capital		
Current year interest		
₹ 25,00,000 x 10% = ₹ 2,50,000	1,25,000	1,25,000
Pre-construction interest		
₹ 25,00,000 x 10% x 9/12 = ₹ 1,87,500		
₹ 1,87,500 allowed in 5 equal installments		
₹ 1,87,500 / 5 = ₹ 37,500 per annum	18,750	18,750
Total deduction under section 24 (B)	1,43,750	1,79,750
Income from house property (A)-(B)	(1,43,750)	(59,750)
Loss under the head "income from house property" of Mr. Kunal (both ground floor and first floor)		(2,03,500)

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

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

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

Annual letting value =	₹ 93,750, being higher of -
	Fair rent = 125,000 x 9 /12 = ₹ 93,750
	Municipal value = 80,000 x 9/12 = ₹ 60,000
Actual rent =	₹ 1,25,000 (₹ 25,000 p.m. for 5 months from July to November, 2013)

Gross annual value = ₹ 1,25,000 (being higher of ALV of ₹ 93,750 and actual rent of ₹ 1,25,000)

5. (a) Computation of written down value of Plant and Machinery of M/s. Amla Ltd.for A.Y. 2014-15

Particulars	₹ (in crores)
Opening written down value (as on 01.04.2013)	50.00
Add: Purchase of plant and machinery during the previous year	106.00
	156.00
Less: Sale proceeds of obsolete plant and machinery sold during the year	0.20
Closing Written Down Value (as on 31.03.2014)	155.80

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

Particulars	₹ (in crores)
Normal Depreciation (₹ 155.80 x 15%)	23.37
Additional Depreciation(Refer Note 2)(₹ 106.00 – ₹ 0.30 - ₹ 0.20) x 20%	21.10
Depreciation on Plant and Machinery	44.47

Computation of deduction under section 32AC for A.Y. 2014-15

Particulars	₹ (in crores)
Deduction under section 32AC (Refer Note 3) (₹ 106.00 – ₹ 0.30 - ₹ 0.20) x 15%	15.825

Notes:-

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

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

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

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

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

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

(i) Plant and machinery of ₹ 0.20 crores used previously for the purpose of business by the seller.

(ii) Plant and machinery of ₹ 0.30 crores installed in office.

Therefore, in the given case, additional depreciation has to be provided only on ₹ 105.50 crore (i.e., ₹ 106.00 crore – ₹ 0.50 crore).

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

The deduction under section 32AC would be in addition to the deduction under section 32 in respect of depreciation and additional depreciation. Further, the deduction under section 32AC would not be reduced to arrive at the WDV of plant and machinery.

The amount of plant or machinery which is previously used by the seller of ₹ 0.20 crores and the plant and machinery of ₹ 0.30 crores installed in office premises has to be deducted while calculating deduction under section 32AC.

(b) (i) Yes. Since his total turnover for the F.Y.2013-14 is below ₹ 1 crore, he is eligible to opt for presumptive taxation scheme under section 44AD in respect of his retail trade business.

(ii) His income from retail trade, applying the presumptive tax provisions under section 44AD, would be ₹ 6,59,680, being 8% of ₹ 82,46,000.

(iii) In case he does not opt for the presumptive taxation scheme under section 44AD, and claims that his income is ₹ 5,85,600 (which is lower than the presumptive business income of ₹ 6,59,680), he has to maintain books of account as required under section 44AA(2) and also get them audited and furnish a report of such audit under section 44AB, since his total income exceeds the basic exemption limit of ₹ 2,00,000.

(iv) In case he opts for the presumptive taxation scheme under section 44AD, the due date would be 31st July, 2014.

In case he does not opt for the presumptive taxation scheme and claims that his income is ₹ 5,85,600 as per books of account, then he has to get his books of account audited under section 44AB, in which case the due date for filing of return would be 30th September, 2014.

6. Computation of capital gains and business income of Ms. Gunjan for A.Y.2014-15

Particulars	₹
Capital Gains	
Fair market value of land on the date of conversion deemed as the full value of consideration for the purposes of section 45(2)	3,20,00,000
Less: Indexed cost of acquisition [₹ 50,00,000 × 852/406]	1,04,92,611
	2,15,07,389
Proportionate capital gains arising during the A.Y. 2014-15 (2,15,07,389 x 5/8)	1,34,42,118
Less: Exemption under section 54EC (restricted to ₹ 50 lakh)	50,00,000
Capital gains chargeable to tax for A.Y.2014-15	84,42,118
Business Income	
Sale price of flats [5 × ₹ 90 lakh]	4,50,00,000
Less: Cost of flats	
Fair market value of land on the date of conversion (3,20,00,000 x 5/8)	2,00,00,000
Cost of construction of flats [5 × ₹ 36 lakh]	1,80,00,000
	70,00,000

Notes:

(1) The conversion of a capital asset into stock-in-trade is treated as a transfer under section 2(47). It would be treated as a transfer in the year in which the capital asset is converted into stock-in-trade.

(2) However, as per section 45(2), the capital gains arising from the transfer by way of conversion of capital assets into stock-in-trade will be chargeable to tax only in the year in which the stock-in-trade is sold.

(3) The indexation benefit for computing indexed cost of acquisition would be available only up to the year of conversion of capital asset to stock-in-trade and not up to the year of sale of stock-in-trade.

(4) For the purpose of computing capital gains in such cases, the fair market value of the capital asset on the date on which it was converted into stock-in-trade shall be deemed to be the full value of consideration received or accruing as a result of the transfer of the capital asset.

In this case, since only 5/8th of stock-in trade (5 flats out of 8 flats) is sold in the P.Y. 2013-14 only proportionate capital gains (i.e. 5/8th) would be chargeable to tax in the A.Y. 2014-15.

(5) On sale of such stock-in-trade (i.e., flats, in this case), business income would arise. The business income chargeable to tax would be the price at which the flats are sold as reduced by the fair market value on the date of conversion of the capital asset (i.e., land) into stock-in-trade and the cost of construction of flats.

(6) In case of conversion of capital asset into stock-in-trade and subsequent sale of stock-in-trade, the period of 6 months, for the purpose of exemption under section 54EC, is to be reckoned from the date of sale of stock-in-trade [*CBDT Circular No.791 dated 2.6.2000]*. In this case, since the investment in bonds of NHAI has been made within 6 months of sale of flats, the same qualifies for exemption under section 54EC, subject to a maximum of ₹ 50 lakh.

7. Tax implications under section 56(2)

(i) Since paintings are included in the definition of "property", therefore, when paintings are received without consideration, the same is taxable under section 56(2)(vii), as the aggregate fair market value of paintings exceed ₹ 50,000.

Therefore, ₹ 2,00,000, being the value of painting gifted by his nephew, would be taxable under section 56(2)(vii) in the hands of Mr. Tejpal, since "nephew" is not included in the definition of "relative" thereunder.

(ii) Any property received without consideration by a HUF from its relative is not taxable under section 56(2)(vii).

Since Verma's son is a member of Verma HUF, he is a "relative" of the HUF. Therefore, if Verma HUF receives any property (shares, in this case) from its member, i.e., Verma's son, without consideration, then, the fair market value of such shares will <u>not</u> be chargeable to tax in the hands of the HUF, since gift received from a "relative" is excluded from the scope of section 56(2)(vii).

(iii) The difference between the aggregate fair market value of shares of a closely held company and the consideration paid for purchase of such shares is deemed as income in the hands of the purchasing company under section 56(2)(viia), if the difference exceeds ₹ 50,000.

Accordingly, in this case, the difference of ₹ 1,80,500 [i.e.,(₹ 105 – ₹ 86) × 9,500] is taxable under section 56(2)(viia) in the hands of Sunshine (P) Ltd.

(iv) The provisions of section 56(2)(viib) are attracted in this case since the shares of a closely held company are issued at a premium (i.e., the issue price of ₹ 18 per share exceeds the face value of ₹ 10 per share) and the issue price exceeds the fair market value of such shares.

The consideration received by the company in excess of the fair market value of the shares would be taxable under section 56(2)(viib).

Therefore, ₹ 84,000 {i.e., (₹ 18 – ₹ 15) x 28,000 shares} shall be the income chargeable under section 56(2)(viib) in the hands of Bijali (P) Ltd.

(v) As per section 145A(b), interest received on enhanced compensation shall be deemed to be the income of the previous year in which it is received, irrespective of the method of accounting followed by the assessee. Therefore, in this case, interest on enhanced compensation received by Mr. Sharan in January, 2014 shall be deemed to be the income of P.Y.2013-14, i.e., the year of receipt, irrespective of the method of accounting followed by him. Such interest is taxable under section 56(2)(viii).

(₹ 1,20,000 + ₹ 1,60,000 + ₹ 2,00,000+ ₹ 60,000)	₹ 5,40,000
Less: Deduction under section 57(iv)@50% of ₹ 5,40,000	₹ 2,70,000
	₹ 2,70,000

8. (a) Tax implications on sale of a building representing a capital asset in the hands of Mr. Suraj, a salaried employee

(i) Tax implications in the hands of Mr. Suraj for A.Y.2014-15

The building represents a capital asset in the hands of Mr. Suraj, a salaried employee. On sale of the building, the provisions of section 50C are attracted and ₹ 159 lakh, being the difference between the stamp duty value on the date of registration (i.e., ₹ 220 lakh) and the purchase price (i.e., ₹ 61 lakh) would be chargeable as short-term capital gains in the hands of Mr. Suraj.

It may be noted that under section 50C, there is no option to adopt the stamp duty value on the date of agreement, even if the date of agreement is different from the date of registration and part of the consideration has been received on or before the date of agreement otherwise than by way of cash.

(ii) Tax implications in the hands of Mr. Rohan for A.Y.2014-15

The building purchased would be a capital asset in the hands of Mr. Rohan, who is engaged in the business of artificial jwellery. The provisions of section 56(2)(vii) would be attracted in the hands of Mr. Rohan who has received immovable property, being a capital asset, for inadequate consideration. For the purpose of section 56(2)(vii), Mr.Rohan can take the stamp duty value on the date of agreement instead of the date of registration since he has paid part of the consideration by a mode other than cash on the date of agreement.

Therefore, ₹ 70 lakh, being the difference between the stamp duty value of the property on the date of agreement (i.e., ₹ 150 lakh) and the actual consideration (i.e., ₹ 80 lakh) would be taxable as per section 56(2)(vii) under the head "Income from other sources" in the hands of Mr. Rohan.

(b) Tax implications if Mr. Suraj is a property dealer

(i) Tax implications in the hands of Mr. Suraj for A.Y.2014-15

If Mr. Suraj is a property dealer who has sold the building in the course of his business, the provisions of section 43CA would be attracted, since the building represents his stock-in-trade and he has transferred the same for a consideration less than the stamp duty value. For the purpose of section

43CA, Mr.Suraj can take the stamp duty value on the date of agreement instead of the date of registration since he has received part of the consideration by a mode other than cash on the date of agreement. Therefore, **₹ 89 lakh**, being the difference between the stamp duty value on the date of agreement (i.e., ₹ 150 lakh) and the purchase price (i.e., ₹ 61 lakh), would be chargeable as **business income** in the hands of Mr. Suraj.

(ii) Tax implications in the hands of Mr. Rohan for A.Y.2014-15

There would be no difference in the taxability in the hands of Mr. Rohan, whether Mr. Suraj is a property dealer or a salaried employee.

Therefore, the provisions of section 56(2)(vii) would be attracted in the hands of Mr. Rohan who has received immovable property, being a capital asset, for inadequate consideration. Consequently, **₹ 70 lakh**, being the difference between the stamp duty value of the property on the date of agreement (i.e., ₹ 150 lakh) and the actual consideration (i.e., ₹ 80 lakh) would be taxable as per section 56(2)(vii) under the head **"Income from other sources"** in the hands of Mr. Rohan.

9. Section 64(1) 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. In this case Smt. Reena received a gift of ₹ 3,50,000 from her husband which she invested in her business. The income to be clubbed in the hands of Smt. Reena's husband for A.Y.2014-15 is computed as under:

Particulars	Smt. Reena's Capital Contribution	Capital Contribution out of gift from husband	Total
	₹	₹	₹
Capital employed as at 1.4.2012	5,00,000	--	5,00,000
Investment on 15.05.2012 out of gift received from her husband		3,50,000	3,50,000
	5,00,000	3,50,000	8,50,000
Profit for F.Y. 2012-13 to be apportioned on the basis of capital employed on the first day of the previous year i.e. on 1.4.2012	2,00,000		2,00,000
Capital employed as at 1.4.2013	7,00,000	3,50,000	10,50,000
Profit for F.Y.2013-14 to be apportioned on the basis of capital employed as at 1.4.2013 (i.e. 2:1)	3,40,000	1,70,000	5,10,000

Therefore, the income to be clubbed in the hands of Smt. Reena's husband for A.Y.2014-15 is ₹ 1,70,000.

10. Computation of total income of Mr. Sitaraman for the A.Y.2014-15

Particulars	₹	₹
Salaries		
Income from salaries	3,22,000	
Less: Loss from house property	1,65,000	1,57,000
Profits and gains of business or profession		
Income from speculation business	26,000	
Less: Loss from retail business set off	26,000	Nil
Capital gains		
Long-term capital gains from sale of residential house	3,60,000	
Less: Loss from retail business set off	1,99,000	1,61,000
Income from other sources		
Income from betting		51,000
Gross total income		3,69,000
Less: Deduction under section 80C for life insurance premium paid (restricted to 10% of ₹ 9 Lakh, being actual capital sum assured)		90,000
Total income		2,79,000

Losses to be carried forward:

Particulars	₹
(1) Loss from retail business (₹ 2,25,000 - ₹ 26,000 - ₹ 1,99,000)	Nil
(2) Loss from specified business covered by section 35AD	31,000

Notes:

(i) Long-term capital gains from sale of listed shares in a recognized stock exchange is exempt under section 10(38). Loss from an exempt source cannot be set off against profits from a taxable source. Therefore, long-term capital loss on sale of listed shares cannot be set-off against long-term capital gains from sale of residential house.

(ii) 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 indefinitely for set-off against profits and gains of any specified business.

(iii) Business loss cannot be set off against salary income. However, the balance business loss of ₹ 1,99,000 (₹ 2,25,000 – ₹ 26,000 set-off against income from speculation business) can be set-off against long-term capital gains of ₹ 3,60,000 from sale of residential house. Consequently, the taxable long-term capital gains would be ₹ 1,61,000.

(iv) Loss from card games can neither be set off against any other income, nor can it be carried forward.

(v) Income from betting is chargeable at a flat rate of 30% under section 115BB and no expenditure or allowance can be allowed as deduction from such income, nor can any loss be set-off against such income.

11. The deduction under section 80CCG shall be available to ;

(i) a new retail investor who complies with the conditions of Rajiv Gandhi Equity Savings Scheme, 2013; and

(ii) whose gross total income for the financial year in which investment is made under the scheme is less than or equal to ₹ 12 lakh.

The question specifies that Mr. Rakesh , Mr. Jaiprakash & Mr. Himesh are new retail investors.

However, since gross total income of Mr. Jaiprakash for the A.Y. 2014-15 exceeds ₹ 12 lakh, he is not eligible for deduction under section 80CCG, even though he is a new retail investor.

Computation of deduction under section 80CCG for A. Y. 2014-15

Particulars	Mr. Rakesh	Mr. Himesh
Investment in listed equity shares	35,000	28,000
Investment in units of equity-oriented fund	25,000	15,000
Total Investment in eligible securities	60,000	43,000
Maximum amount of investment eligible for deduction under section 80CCG(1)	50,000	43,000
Deduction under section 80CCG for A.Y. 2014-15 (50% of Above)	25,000	21,500

Note – In case Mr. Himesh sells all the listed shares in January 2015, the amount of ₹ 14,000 (50% of ₹ 28,000), being the deduction allowed to him under section 80CCG in A.Y. 2014-15, would be subject to tax in the A.Y. 2015-16, since the condition of minimum fixed lock-in period upto 31.03.2015 has been violated in this case. However in the case of Mr. Jaipraksh, since deduction under section 80CCG was not allowed during the A.Y. 2014-15 on account of his gross total income exceeding ₹ 12 lakh, no amount invested in that year can be subject to tax in the A.Y. 2015-16, being the year of violation of condition, even though, the units are sold within the fixed lock-in period (Refer Notification No. 94/2013, dated 18.12.2013 given in Part I of this RTP).

12. Computation of total income of Dr. Sonia for A.Y. 2014-15

	Particulars	₹	₹	₹
I	**Income from Salary**			
	Salary (₹ 15,000 x 12)			1,80,000
II	**Income from house property**			
	Gross Annual Value (GAV)		36,000	
	Less : Municipal taxes paid		2,800	
	Net Annual Value (NAV)		33,200	
	Less : Deduction under section 24 @ 30% of ₹ 31,200		9,960	23,240
III	**Income from profession**			
	Net profit as per Income and Expenditure account		3,13,660	
	Less : Items of income to be treated separately			
	(i) Rent received	36,000		
	(ii) Dividend from units of UTI	9,400		
	(iii) Winning from game show on T.V. (net of TDS)	36,400		
	(iv) Income tax refund	5,450	87,250	
			2,26,410	
	Less : Allowable expenditure			
	Depreciation on Clinic equipments			
	on ₹ 4,50,000 @ 15%	67,500		
	on ₹ 2,25,000 @ 7.5% (On equipments acquired during the year which were put to use for less than 180 days; she is entitled to depreciation @ 7.5% being, 50% of 15%)	16,875		
	Additional deduction of 75% for amount paid to scientific research association (Since weighted deduction of 175% is available in respect of such payment)	1,35,000	2,19,375	
			7,035	
	Add: Items of expenditure not allowable			

	while computing business income			
	(i) Rent for her residential accommodation included in Income and Expenditure A/c	37,000		
	(ii) Municipal tax paid relating to residential house at Gwalior included in administrative expenses	2,800	39,800	46,835
IV	Income from other sources			
	(a) Interest on income-tax refund		650	
	(b) Dividend from UTI [Exempt under section 10(35)]		Nil	
	(c) Winnings from the game show on T.V. (₹ 36,400 + ₹ 15,600)		52,000	52,650
	Gross Total Income			3,02,725
	Less: Deductions under Chapter VI A:			
	(a) Section 80C - Tuition fee paid to university for full time education of her daughter		80,000	
	(b) Section 80D - Medical insurance premium (Maximum of ₹ 20,000 allowed as deduction since, she is a senior citizen)		20,000	
	(c) Deduction under section 80E - Interest on loan taken for higher education is deductible		75,000	1,75,000
	Total income			1,27,725

Notes:

(i) The principal amount received towards income-tax refund will be excluded from computation of total income. Interest received will be taxed under the head "Income from other sources".

(ii) Winnings from game show on T.V. should be grossed up for the chargeability under the head "Income from other sources" (₹ 36,400 + ₹ 15,600). Thereafter, while computing tax liability, TDS of ₹ 15,600 should be deducted to arrive at the tax payable. Winnings from game show are subject to tax @30% as per section 115BB.

(iii) Since Dr. Sonia is staying in a rented premise in Gwalior itself, she would not be eligible for deduction u/s 80GG, since she owns a house in Gwalior which she has let out.

(iv) It is assumed that clinical equipments do not include life saving medical equipments eligible for depreciation @40%.

13. (a) (i) Since the sale consideration of house property exceeds ₹ 50 lakh, Mr. Siddharth is required to deduct tax at source under section 194-IA. The tax to be deducted under section 194IA would be ₹ 80,000, being 1% of ₹ 80 lakh.

TDS provisions under section 194-IA are not attracted in respect of transfer of rural agricultural land.

(ii) As per section 194J, liability to deduct tax is attracted only in case the payment made as fees for professional services and royalty, individually, exceeds ₹ 30,000 during the financial year. In the given case, since, the individual payment for fee of ₹ 28,000 for professional services and royalty of ₹ 25,000 is less than ₹ 30,000 each, there is no liability to deduct tax at source. It is assumed that no other payment towards fees for professional services and royalty were made during the year to Mr. Varun.

(iii) Section 194-I, which requires the deduction of tax at source on payment of rent exceeding ₹ 1,80,000 per annum is applicable to all persons other than individuals and HUF's, who are not subject to tax audit in the immediately preceding financial year. Therefore, the TDS provisions under section 194-I are applicable in respect of rental payments made by a bank. However, under section 196, payments made to Government are exempt from the application of provisions of tax deduction at source.

Hence, Punjab National Bank is not required to deduct tax at source on payment of ₹ 1,00,000 per month as rent to Central Government.

(iv) As per section 194LA, any person responsible for payment to a resident, any sum in the nature of compensation or consideration on account of compulsory acquisition under any law, of any immovable property, is responsible for deduction of tax at source if such payment or the aggregate amount of such payments to the resident during the financial year exceeds ₹ 2,00,000.

In the given case, no liability to deduct tax at source is attracted as the payment made does not exceed ₹ 2,00,000.

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

Particulars	₹
Income from other sources	
Interest earned from Non-resident (External) Account ₹ 3,06,000 [Exempt under section 10(4)(ii), assuming that Mr. Rajveer has been permitted by RBI to maintain the aforesaid account]	Nil
Interest on bank fixed deposit	25,000

Interest on savings bank account	9,600
Gross Total Income	34,600
Less: Deduction under section 80TTA – Interest on saving bank account	9,600
Total Income	25,000

An individual is required to furnish a return of income under section 139(1) if his total income, before giving effect to the provisions of chapter VI-A, exceeds the maximum amount not chargeable to tax i.e. ₹ 2,00,000 (for A.Y. 2014-15). In this case, since Mr. Rajveer's total income of ₹ 34,600 before giving effect to deduction under section 80TTA, is less than the basic exemption limit of ₹ 2 lakh, he is not required to file a return of income.

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

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

(ii) signing authority in any account located outside India

is required to file a return of income in the prescribed form compulsorily on or before the due date of filing the return of income, irrespective of the fact that his total income does not exceed the basic exemption limit.

Since Mr. Rajveer owns a house in London, he has to compulsorily file his return of income for A.Y 2014-15 on or before 31st July 2014, irrespective of the fact that his total income is less than the basic exemption limit of ₹ 2 lakh.

14. (i) In case where the taxable services are provided by any person located in a non-taxable territory and are received by any person located in the taxable territory, person liable to pay service tax is the recipient of such service under reverse charge mechanism. Thus, in the given case, X Techies Ltd. is liable to pay service tax on the taxable service imported by it.

(ii) As per the Point of Taxation Rules, 2011, the point of taxation in respect of the persons required to pay tax under reverse charge mechanism is the date on which payment is made provided payment is made within a period of 6 months from the date of invoice.

Since in the given case, X Techies Ltd. has made the payment within 6 months from the date of the invoice, the point of taxation is the date of payment i.e., 10.12.2013.

(iii) The amount of R&D cess payable is allowed as a deduction from the service tax payable on the taxable service involving the import of technology provided:-

(i) said amount of R&D cess is paid at the time or before the payment for the service subject to a maximum of 6 months from the date of invoice and

(ii) records of R&D cess are maintained for establishing the linkage between the invoice and the R&D cess payment challan.

Since both the aforesaid conditions are fulfilled, X Techies Ltd. is eligible for said exemption. Therefore, service tax payable by X Techies Ltd. would be computed as under:

Particulars	(₹)
Service tax (₹12,00,000 × 12.36%)	1,48,320
Less: Research and development cess paid	60,000
Net service tax liability	88,320

15. The view taken by BTR Association is not valid in law. As per section 65B(44) of the Finance Act, 1994, service means, *inter alia*, any activity for consideration carried out by a person for another. The term 'person' is not restricted to a natural person. The definition of person under section 65B(37), includes, *inter alia*, body of individuals, whether incorporated or not.

    Thus, BTR Association is a person as it is a body of individuals and services provided by it would come under purview of definition of 'service' under section 65B(44) of the Finance Act, 1994.

16. Computation of service tax leviable on services received/availed by Ms. Kohana

Particulars	Value of taxable service received (₹)	Service tax @ 12.36% (₹)
Amount deposited in the saving bank account and interest earned (Note-1)	-	-
Services of mobile network operator (Note-2)	2,000.00	247
Visit to an orthopaedician on complaint of severe backache (Note-3)	-	-
Beauty treatment services (Note-2)	6,000.00	742
Total service tax payable on services availed/received		989

Notes:

1. Amount of ₹ 1,00,000 deposited in Savings Bank Account is a transaction in money which is specifically excluded from the definition of service under section 65B(44) of the Finance Act, 1994. Further, ₹ 5,000 received by Ms. Kohana as interest on deposits will not be liable to service tax as services by way of extending deposits in so far as the consideration is represented by way of interest are covered in the negative list of services [Section 66D of the Finance Act, 1994].

2. Service tax is leviable on services of a mobile network operator and beauty treatment services received from a beauty salon as such services are neither covered under negative list of services nor under any exemption notification.

3. Health care service provided, *inter alia,* by an authorized medical practitioner is exempt vide mega exemption *Notification No. 25/2012 ST dated 20.06.2012*. Health care service means any service by way of diagnosis or treatment or care for *inter alia* any illness in any recognized system of medicines in India. Allopathy is a recognized system of medicine in India and a MBBS, MS doctor is an authorized medical practitioner. So, visit to an orthopaedician on complaint of severe backache is not taxable.

17. In the given case, since the invoice is issued within the prescribed period of 30 days from the date of completion of provision of service, the point of taxation, as per rule 3 of the Point of Taxation Rules, 2011, shall be the:

(a) date of invoice (i.e. 20.03.2014)

or

(b) date of receipt of payment (i.e. 15.03.2014) [Refer note below]

whichever is earlier, i.e. 15.03.2014.

Note: Date of payment is the :-

(1) date on which the payment is entered in the books of account (i.e. 15.03.2014)

or

(2) date on which the payment is credited to the bank account of the person liable to pay tax (i.e. 25.03.2014)

whichever is earlier, i.e. 15.03.2014 [Rule 2A of the Point of Taxation Rules, 2011].

18. Computation of service tax liability of Well-Being Nursing Home for the month of February, 2014

Particulars	(₹) (in lakh)
Palliative care for terminally ill patients at patient's home [Note- 1(a)]	-
Services provided by cord blood bank by way of preservation of stem cells. [Note-2]	-
Hair transplant services [Note-1(b)]	1,00.000
Ambulance services to transport critically ill patients from various locations to nursing home [Note-1(c)]	-
Naturopathy treatments [Note-1(d)]	-
Plastic surgery to restore anatomy of a child affected due to an accident	-

[Note-1(e)]	
Pranic healing treatments [Note-1(f)]	1,20.000
Mortuary services [Note 3]	-
Value of taxable service	2,20.000
Service tax @ 12% [₹ 220 lakh × 12%]	26.400
Education cess @ 2% [₹ 26.40 lakh × 2%]	0.528
Secondary and higher education cess @ 1% [₹ 26.40 lakh ×1%]	0.264
Service tax liability	27.192

Notes:

(1) Health care services provided by, *inter alia,* a clinical establishment in any recognized system of medicines in India is exempt from service tax vide *Mega Exemption Notification No. 25/2012 ST dated 20.06.2012*.

(a) Health care service means any service by way of diagnosis or treatment or care for illness, injury, deformity, abnormality or pregnancy in any recognized system of medicines in India. It is immaterial whether such service is provided at the clinical establishment or at the home of the patient or at any other place. Thus, palliative care for terminally ill patients at patient's home is eligible for exemption.

(b) Hair transplant services are specifically excluded from the health care services, and thus are not eligible for exemption.

(c) Services by way of transportation of the patient to and from a clinical establishment are specifically included in the health care services. Thus, ambulance services to transport critically ill patients from various locations to nursing home are eligible for exemption.

(d) Since naturopathy is a recognized system of medicine in terms of section 2(h) of the Clinical Establishments Act, 2010, it would be eligible for exemption.

(e) Health care service does not include *inter alia* cosmetic or plastic surgery, except when undertaken to restore or to reconstruct anatomy or functions of body affected due to congenital defects, developmental abnormalities, injury or trauma. Hence, plastic surgery to restore anatomy of a child affected due to an accident will be eligible for exemption.

(f) Since pranic healing treatment is not a recognized system of medicine in terms of section 2(h) of the Clinical Establishments Act, 2010, it would not be eligible for exemption.

(2) Services provided by cord blood banks by way of preservation of stem cells or any other service in relation to such preservation are also exempt from service tax vide *Mega Exemption Notification No. 25/2012 ST dated 20.06.2012.*

(3) Mortuary services are covered under negative list of services under section 66D of the Finance Act, 1994. Hence, the same are not liable to service tax.

19. No, Shyam is not liable to pay service tax on the transaction entered into by him with Mohan Brothers. The transfer of tempos by way of hiring along with right to use is a deemed sales as per article 366(29A) of the Constitution of India. Charging section 66B of the Finance Act, 1994 stipulates that service tax is leviable on the value of all 'services' provided by one person to another. However, transfer, delivery or supply of any goods which is deemed to be a sale within the meaning of article 366(29A) of the Constitution is specifically excluded from the definition of 'service' under section 65B(44) of the Finance Act, 1994.

Therefore, the transaction entered into by Shyam with Mohan Brothers is not chargeable to service tax. Instead, VAT is leviable on the same.

20. As per rule 3(4) of CENVAT Credit Rules, 2004, while paying excise duty or service tax, CENVAT credit can be utilised only to the extent such credit is available on the last day of the month or quarter for payment of duty or tax relating to that month or the quarter. Thus, CENVAT credit available as on 31.01.2014 can only be utilized by LMN (Pvt.) Ltd. to discharge service tax liability of the month of January.

Further, as per rule 3(7), credit of NCCD can be utilized towards payment of NCCD only. Therefore, CENVAT credit of ₹ 15,000 relating to NCCD cannot be utilized by LMN (Pvt.) Ltd. towards payment of its service tax liability.

In view of the above provisions, CENVAT credit available with LMN (Pvt.) Ltd. as on 31.01.2014 will be computed as under:

Particulars	CENVAT credit			
	Excise duty		Service tax (₹) [Input services]	Total (₹)
	Inputs (₹)	Capital goods (₹)		
Balance as on 01.01.2014	50,000	1,00,000	15,000	1,65,000
Inputs received on 10.01.2014	30,000			30,000
Inputs received on 15.01.2014	50,000			50,000
Capital goods received on 20.01.2014 [Upto 50% of the excise duty paid can be availed as CENVAT credit in respect of capital goods in the year of purchase.]		35,000		35,000

Invoices (for input services) dated 23.01.2014 received same day			35,000	35,000
Balance as on 31.01.2014	1,30,000	1,35,000	50,000	3,15,000

Computation of service tax payable in cash by LMN (Pvt.) Ltd.

Particulars	(₹)
Service tax liability for the month of January, 2014	3,50,000
Less: CENVAT credit available as on 31.01.2014 [(₹3,15,000 - ₹15,000) as credit of NCCD cannot be utilized to pay service tax]	3,00,000
Service tax to be paid in cash	50,000

21. (a) Computation of central excise duty payable

Particulars	(₹)
Price of machine excluding taxes and duties	10,00,000
Installation and erection expenses [Note 1]	-
Special packing charges [Note 2]	12,500
Design and engineering charges of the machine [Note 2]	40,000
Dharmada charged in the invoice [Note 3]	10,000
Assessable value	10,62,500
Excise duty payable @ 12.36% [inclusive of 3% education cesses]	1,31,325

Notes:

1. Installation and erection expenses have not been included in the assessable value as after the installation and erection, machine has been permanently affixed to earth and thus, it has resulted in an immovable property.
2. Special packing charges and design and engineering charges have been included in the assessable value as such payments are 'in connection with sale'.
3. Dharmada charged in the invoice and recovered from the customer has been included in the assessable value.

(b) If imported goods are similar to goods covered under section 4A of the Central Excise Act, 1944, CVD is payable on the basis of MRP printed on the package less abatement as permissible. Therefore, CVD payable by Sneha Subramanian will be computed as under:

Particulars	(₹)
Maximum retail price [8,000 pieces × 30]	2,40,000
Less: Abatement @ 30%	72,000
Assessable value	1,68,000
CVD @ 12% of ₹ 1,68,000 [Education cesses on CVD are exempt]	20,160

22. Computation of Net VAT payable by Rainbow & Co.:-

Particulars	(₹)
Output VAT payable:	
Sale of goods at 4% VAT (₹ 8,00,000 × 4%) (manufactured out of exempted material)	32,000
Sale of finished goods at 12% VAT (₹ 10,00,000 × 12%)	1,20,000
Sale of raw materials purchased at 4% VAT (₹ 5,00,000 × 4%)	20,000
Total (A)	1,72,000
Input tax credit available:	
Purchase of raw material @ 4% VAT 40% of (₹ 20,00,000 × 4%) [Note – 1]	32,000
Purchase of raw material @ 12% VAT including purchases used for manufacturing capital goods produced (12% of ₹ 10,00,000) [Note – 2]	1,20,000
Total (B)	1,52,000
Net VAT payable (A) – (B)	20,000

Notes:

1. Input tax credit in respect of goods used to produce exempted goods is not allowed. Hence, 60% of the input tax credit has been disallowed on goods purchased at 4% VAT which are utilized to produce exempted goods.
2. Input tax credit on raw materials is allowed even if the same has been consumed to produce capital goods. Hence, full input tax credit on goods purchased at 12% VAT has been allowed.

23. Computation of taxable turnover of Mediatek Pvt. Ltd.

Particulars	(₹)
Total sales	2,00,00,000
Less: Goods returned by Amit (deductible as returned within 6 months)	1,50,000

Less: Goods rejected by Sumit after six months (Refer note below)	45,000
Less: Goods returned by Shyam (not deductible since returned after six months)	-
Turnover including CST	1,98,05,000
Less : Central sales tax $= 1,98,05,000 \times \frac{4}{104}$ (Rounded off)	7,61,731
Taxable turnover	1,90,43,269

Note: The period of six months for return of goods is not applicable in respect of rejected goods as it is a case of un-fructified sale.