PAPER – 1: ACCOUNTING

PART – I: ANNOUNCEMENTS STATING APPLICABILITY & NON-APPLICABILITY FOR NOVEMBER, 2015 EXAMINATION

A. Applicable for November, 2015 examination

(i) Companies Act, 2013

The relevant Sections of the Companies Act, 2013 notified up to 31st March, 2015 will be applicable for Nov., 2015 Examination.

(ii) Dividend Distribution Tax

(a) With effect from 1st Oct, 2014 dividend and income distribution tax is leviable on gross dividend / income and not on the net dividend / income distributed to shareholders and unit holders as per Income- tax Act, 1961.

(b) The rate of DDT is fifteen per cent (excluding surcharge of 12% plus secondary and higher education cess is (2+1) 3%).

B. Ind ASs issued by the Ministry of Corporate Affairs are not applicable for November, 2015 examination

PART – II : QUESTIONS AND ANSWERS

QUESTIONS

Preparation of Financial Statements of Companies

1. From the following particulars furnished by Alpha Ltd., prepare the Balance Sheet as on 31st March 2015 as required by Part I, Schedule III of the Companies Act, 2013.

Particulars		*Debit ₹*	*Credit ₹*
Equity Share Capital (Face value of ₹ 100 each)			50,00,000
Call in Arrears		5,000	
Land & Building		27,50,000	
Plant & Machinery		26,25,000	
Furniture		2,50,000	
General Reserve			10,50,000
Loan from State Financial Corporation			7,50,000
Inventory:			
Raw Materials	2,50,000		
Finished Goods	10,00,000	12,50,000	
Provision for Taxation			6,40,000

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Trade receivables		10,00,000	
Short term Advances		2,13,500	
Profit & Loss Account			4,33,500
Cash in Hand		1,50,000	
Cash at Bank		12,35,000	
Unsecured Loan			6,05,000
Trade payables (for Goods and Expenses)			8,00,000
Loans & advances from related parties			2,00,000

The following additional information is also provided:

(i) 10,000 Equity shares were issued for consideration other than cash.

(ii) Trade receivables of ₹ 2,60,000 are due for more than 6 months.

(iii) The cost of the Assets were:

Building ₹ 30,00,000, Plant & Machinery ₹ 35,00,000 and Furniture ₹ 3,12,500

(iv) The balance of ₹ 7,50,000 in the Loan Account with State Finance Corporation is inclusive of ₹ 37,500 for Interest Accrued but not Due. The loan is secured by hypothecation of Plant & Machinery.

(v) Balance at Bank includes ₹ 10,000 with Omega Bank Ltd., which is not a Scheduled Bank.

(vi) The following appropriations have been proposed by the Board of directors out of profits for the year:

(a) Transfer ₹ 20,000 to general reserve

(b) Declared dividend of 5% on the paid up capital.

Cash Flow Statements

2. J Ltd. presents you the following information for the year ended 31st March, 2015:

		(₹ in lacs)
(i)	Net profit before tax provision	36,000
(ii)	Dividend paid	10,202
(iii)	Income-tax paid	5,100
(iv)	Book value of assets sold	222
	Loss on sale of asset	48
(v)	Depreciation debited to P & L account	24,000
(vi)	Capital grant received - amortized to P & L A/c	10

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(vii)	Book value of investment sold Profit on sale of investment	33,318 120
(viii)	Interest income from investment credited to P & L A/c	3,000
(ix)	Interest expenditure debited to P & L A/c	12,000
(x)	Interest actually paid (Financing activity)	13,042
(xi)	Increase in working capital [Excluding cash and bank balance]	67,290
(xii)	Purchase of fixed assets	22,092
(xiii)	Expenditure on construction work	41,688
(xiv)	Grant received for capital projects	18
(xv)	Long term borrowings from banks	55,866
(xvi)	Provision for Income-tax debited to P & L A/c	6,000
	Cash and bank balance on 1.4.2014	6,000
	Cash and bank balance on 31.3.2015	8,000

You are required to prepare a cash flow statement as per AS-3 (Revised).

Profit or Loss Pre and Post Incorporation

3. The partnership of Surya Agencies decided to convert the partnership into Private Limited Company named Sohna Company Pvt. Ltd. with effect from 1st January, 2014. The consideration was agreed at ₹ 2,34,00,000 based on firm's Balance Sheet as on 31st December, 2013. However, due to some procedural difficulties, the company could be incorporated only on 1st April, 2014. Meanwhile, the business was continued on behalf of the company and the consideration was settled on that day with interest at 12% p.a. The same books of accounts were continued by the company, which closed its accounts for the first time on 31st March, 2015 and prepared the following summarized Profit and Loss account:

		₹		₹
To	Cost of goods sold	3,27,60,000	By Sales	4,68,00,000
To	Salaries	23,40,000		
To	Depreciation	3,60,000		
To	Advertisement	14,04,000		
To	Discount	23,40,000		
To	Managing Director's remuneration	1,80,000		
To	Miscellaneous office expenses	2,40,000		
To	Office cum showroom rent	14,40,000		

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To Interest	19,02,000		
To Profit	38,34,000		
	4,68,00,000		4,68,00,000

The company's only borrowing was a loan of ₹ 1,00,00,000 at 12% p.a. to pay the purchase consideration due to the firm and for working capital requirements. The company was able to double the monthly average sales of the firm from 1st April, 2014, but the salaries trebled from the date. It had to occupy additional space from 1st July, 2014 for which rent was ₹ 60,000 per month.

Prepare a statement showing apportionment of costs and revenue between pre-incorporation and post-incorporation periods.

Accounting for Bonus Issue

4. Following items appear in the Trial Balance of Saral Ltd. as on 31st March, 2015:

Particulars	*Amount*
4,500 Equity Shares of ₹100 each	4,50,000
Capital Reserve (including ₹40,000 being profit on sale of Plant)	1,00,000
Securities Premium	40,000
Capital Redemption Reserve	30,000
General Reserve	1,05,000
Profit and Loss Account (Cr. Balance)	45,000

The company decided to issue to equity shareholders bonus shares at the rate of 1 share for every 3 shares held. Company decided that there should be the minimum reduction in free reserves. Pass necessary Journal Entries in the books Saral Ltd.

Internal Reconstruction of a Company

5. The following is the summarized Balance Sheet of Rocky Ltd. as at March 31, 2015:

	₹ in lacs
Liabilities	
Fully paid equity shares of ₹ 10 each	500
Capital Reserve	6
12% Debentures	400
Debenture Interest Outstanding	48
Trade payables	165
Directors' Remuneration Outstanding	10
Other Outstanding Expenses	11

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Provisions	33
	1,173
Assets	
Goodwill	15
Land and Building	184
Plant and Machinery	286
Furniture and Fixtures	41
Inventory	142
Trade receivables	80
Cash at Bank	27
Discount on Issue of Debentures	8
Profits and Loss Account	390
	1,173

The following scheme of internal reconstruction was framed, approved by the Tribunal, all the concerned parties and implemented:

(i) All the equity shares be converted into the same number of fully-paid equity shares of ₹ 2.50 each.

(ii) Directors agree to forego their outstanding remuneration.

(iii) The debentureholders also agree to forego outstanding interest in return of their 12% debentures being converted into 13% debentures.

(iv) The existing shareholders agree to subscribe for cash, fully paid equity shares of ₹ 2.50 each for ₹ 125 lacs.

(v) Trade payables are given the option of either to accept fully-paid equity shares of ₹ 2.50 each for the amount due to them or to accept 80% of the amount due in cash. Trade payables for ₹ 65 lacs accept equity shares whereas those for ₹ 100 lacs accept ₹ 80 lacs in cash in full settlement.

(vi) The Assets are revalued as under:

	₹ in lacs
Land and building	230
Plant and Machinery	220
Inventory	120
Trade receivables	76

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Pass Journal Entries for all the above mentioned transactions and draft the company's Balance Sheet immediately after the reconstruction.

Amalgamation of Companies

6. The summarized Balance Sheet of M/s. A Ltd. and M/s B Ltd. as on 31.03.2015 were is as under:

Liabilities	*A Ltd.* ₹	*B Ltd.* ₹	*Assets*	*A Ltd.* ₹	*B Ltd.* ₹
Share Capital:			Freehold Property	3,00,000	2,40,000
40,000 Equity Share			Plant & Machinery	60,000	40,000
of ₹ 10 each, Fully paid	4,00,000	-	Motor Vehicle Trade	30,000	20,000
30,000 Equity Shares			Receivables	2,00,000	80,000
of ₹ 10 each, Fully paid	-	3,00,000	Inventory	2,30,000	1,80,000
General Reserve	2,40,000	-	Cash at Bank	80,000	40,000
Profit & Loss Account	50,000	50,000			
Trade Payables	2,10,000	1,30,000			
6% Debentures (₹100)	-	1,20,000			
	9,00,000	6,00,000		9,00,000	6,00,000

M/s. A Ltd. and M/s. B Ltd. carry on business of similar nature and they agreed to amalgamate. A new Company, M/s. AB Ltd. is formed to take over the Assets and Liabilities of M/s. A Ltd. and M/s. B Ltd. on the following basis:

Assets and Liabilities are to be taken at Book Value, with the following exceptions:

(a) Goodwill of M/s. A Ltd. and M/s. B Ltd. is to be valued at ₹ 1,40,000 and ₹ 40,000 respectively.

(b) Plant & Machinery of M/s. A Ltd. are to be valued at ₹ 1,00,000.

(c) The Debentures of M/s. B Ltd. are to be discharged at premium of 5% by the issue of 10% Debentures of M/s. AB Ltd. at par (₹ 100 each).

You are required to:

(i) Compute the basis on which shares in M/s. AB Ltd. will be issued to Shareholders of the existing Companies assuming nominal value of each share of M/s. AB Ltd. is ₹ 10.

(ii) Draw up a Balance Sheet of M/s. AB Ltd. as on 1st April, 2015, when Amalgamation is completed.

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(iii) Pass Journal entries in the Books of M/s. AB Ltd. for acquisition of M/s. A Ltd. and M/s. B Ltd.

Average Due Date

7. Harish has the following bills due on different dates. It was agreed to settle the total amount due by a single cheque payment. Find the date of the cheque.

   (i) ₹ 5,000 due on 5.3.2015

   (ii) ₹ 7,500 due on 7.4.2015

   (iii) ₹ 6,000 due on 17.7.2015

   (iv) ₹ 8,000 due on 14.9.2015

Account Current

8. From the following particulars prepare a account current, as sent by Mr. Ram to Mr. Laxman as on 31st October 2014 by means of product method charging interest @ 5% p.a.

2014	*Particulars*	₹
1st July	Balance due from Siva	750
15th August	Sold goods to Siva	1,250
20th August	Goods returned by Siva	200
22nd Sep	Siva paid by cheque	800
15th Oct	Received cash from Siva	500

Self – Balancing Ledgers

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

	₹
Balance as on 1.4.2015	
Debit balances in Debtors ledger	2,46,200
Credit balances in Debtors ledger	3,400
Transactions during the month of April, 2015	
Credit sales	9,74,900
Sales return	21,700
Cash received from debtors	8,62,100
Discount allowed to debtors	39,200
Bills receivable received from debtors	51,200
Bills receivable dishonoured	3,500

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Bills payable given to suppliers	27,000
Credit balance in Debtors ledger on 30.4.2015	5,200

Financial Statements of Not-For-Profit Organizations

10. Following is the Receipts and Payments Account of Mayur Club (not registered under Companies Act, 2013) for the year ended 31st March, 2015:

Receipts	₹	*Payments*	₹
Opening balance (1.4.2014)		Payments:	
Cash on hand	39,100	Sports materials	3,04,500
Cash at bank	50,000	Salaries	3,15,000
Receipts:		Equipment purchased on 1.10.2014	60,000
Subscriptions		Bank fixed deposits on 31.3.2015	1,50,000
For the year 2013-14	18,000	Rent	1,48,500
For the year 2014-15	9,63,000	Ground maintenance	22,120
For the year 2015-16	4,500	Insurance	38,400
Interest on bank		Stationery	3,450
Fixed deposits @10%	45,000	Sundry expenses	5,880
		Closing balance as on 31.3.2015	
		Cash on hand	31,750
		Cash at bank	40,000
	11,19,600		11,19,600

Following additional information is provided to you:

(i) The club has 220 members. The annual subscription is ₹ 4,500 per member.

(ii) Depreciation to be provided on furniture at 10% p.a. and on sports equipment at 15% p.a.

(iii) On 31st March, 2015, stock of sports material in hand (after members use during the year) is valued at ₹ 78,000 and stock of stationery at ₹ 3,150. Rent for 1 month is outstanding. Unexpired insurance amounts to ₹ 9,600.

(iv) On 31st March, 2014 the club had the following assets:

Furniture	₹	2,70,000
Sports equipment	₹	1,80,000
Bank fixed deposit	₹	4,50,000
Stock of stationery	₹	1,500

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Stock of sports material	₹	73,500
Unexpired insurance	₹	8,400
Subscription in arrear	₹	22,500

Note: There was no liability on 31.3.2014.

You are required to prepare:

(i) Income and Expenditure Account; and

(ii) Balance Sheet as at 31st March, 2015.

Accounts from Incomplete Records

11. Following are the incomplete information of Moonlight Traders:

The following balances are available as on 31.03.2013 and 31.03.2014.

Balances	*31.03.2013*	*31.03.2014*
Land and Building	5,00,000	5,00,000
Plant and Machinery	2,20,000	3,30,000
Office equipment	1,05,000	85,000
Debtors (before charging for Bad debts)	?	2,25,000
Creditors for purchases	95,000	?
Creditors for office expenses	20,000	15,000
Stock	?	65,000
Long term loan from SBI @ 12%.	1,60,000	100,000
Bank	25,000	?

Other Information	In ₹
Collection from debtors	9,25,000
Payment to creditors for purchases	5,25,000
Payment of office expenses (excluding interest on loan)	42,000
Salary paid	32,000
Selling expenses	15,000
Cash sales	2,50,000
Credit sales (80% of total sales)	
Credit purchases	5,40,000
Cash purchases (40% of total purchases)	
GP Margin at cost plus 25%	

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Discount Allowed	5,500
Discount Received	4,500
Bad debts (2% of closing debtors)	
Depreciation to be provided as follows:	
Land and Building	5%
Plant and Machinery	10%
Office Equipment	15%

Other adjustments:

(i) On 01.10.13 they sold machine having Book Value ₹ 40,000 (as on 31.03.2013) at a loss of ₹ 15,000. New machine was purchased on 01.01.2014.

(ii) Office equipment was sold at its book value on 01.04.2013.

(iii) Loan was partly repaid on 31.03.14 together with interest for the year.

Prepare Trading, P & L A/c and Balance Sheet as on 31.03.2014.

Hire -Purchase

12. A firm acquired two tractors under hire purchase agreements, details of which were as follows:

Date of Purchase	*Tractor A* *1st April, 2013* *(₹)*	*Tractor B* *1st Oct., 2013* *(₹)*
Cash price	14,000	19,000

Both agreements provided for payment to be made in twenty-four monthly instalments (of ₹ 600 each for Tractor A and ₹ 800 each for Tractor B), commencing on the last day of the month following purchase, all instalments being paid on due dates.

On 30th June, 2014, Tractor B was completely destroyed by fire. In full settlement, on 10th July, 2014 an insurance company paid ₹ 15,000 under a comprehensive policy. Any balance on the hire purchase company's account in respect of these transactions was to be written off.

The firm prepared accounts annually to 31st December and provided depreciation on tractors on a straight-line basis at a rate of 20 per cent per annum rounded off to nearest ten rupees, apportioned as from the date of purchase and up to the date of disposal.

You are required to record these transactions in the following accounts, carrying down the balances on 31st December, 2013 and 31st December, 2014:

(a) Tractors on hire purchase.

(b) Provision for depreciation of tractors.

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(c) Disposal of tractors.

Investment Accounts

13. Smart Investments made the following investments in the year 2013-14:

12% State Government Bonds having face value ₹ 100

Date	*Particulars*
01.04.2013	Opening Balance (1200 bonds) book value of ₹ 126,000
02.05.2013	Purchased 2,000 bonds @ ₹ 100 cum interest
30.09.2013	Sold 1,500 bonds at ₹ 105 ex interest

Interest on the bonds is received on 30th June and 31st Dec. each year.

Equity Shares of X Ltd.	
15.04.2013	Purchased 5,000 equity shares @ ₹ 200 on cum right basis Brokerage of 1% was paid in addition (Face Value of shares ₹ 10)
03.06.2013	The company announced a bonus issue of 2 shares for every 5 shares held.
16.08.2013	The company made a rights issue of 1 share for every 7 shares held at ₹ 250 per share. The entire money was payable by 31.08.2013.
22.8.2013	Rights to the extent of 20% was sold @ ₹ 60. The remaining rights were subscribed.
02.09.2013	Dividend @ 15% for the year ended 31.03.2013 was received on 16.09.2013
15.12.2013	Sold 3,000 shares @ ₹ 300. Brokerage of 1% was incurred extra.
15.01.2014	Received interim dividend @ 10% for the year 2013-14
31.03.2014	The shares were quoted in the stock exchange @ ₹ 220

Prepare Investment Accounts in the books of Smart Investments. Assume that the average cost method is followed.

Insurance Claim

14. On 2.6.2014 the stock of Mr. Black was destroyed by fire. However, following particulars were furnished from the records saved:

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	₹
Stock at cost on 1.4.2013	1,35,000
Stock at 90% of cost on 31.3.2014	1,62,000
Purchases for the year ended 31.3.2014	6,45,000
Sales for the year ended 31.3.2007	9,00,000
Purchases from 1.4.2014 to 2.6.2014	2,25,000
Sales from 1.4.2014 to 2.6.2014	4,80,000

Sales upto 2.6.2014 includes ₹ 75,000 being the goods not dispatched to the customers. The sales invoice price is ₹ 75,000.

Purchases upto 2.6.2014 includes a machinery acquired for ₹ 15,000.

Purchases upto 2.6.2014 does not include goods worth ₹ 30,000 received from suppliers, as invoice not received upto the date of fire. These goods have remained in the godown at the time of fire. The insurance policy is for ₹ 1,20,000 and it is subject to average clause. Ascertain the amount of claim for loss of stock.

Partnership - Admission of a Partner

15. Anuj, Ayush and Piyush are in partnership sharing profits and losses in the ratio 2 : 2 : 1. Their Balance Sheet as on 31.3 .2014 is as follows:

Liabilities	₹	₹	*Assets*	₹
Capital accounts:			Fixed assets:	
Anuj	3,75,000		Plant	7,87,000
Ayush	2,80,000		Current assets:	
Piyush	2,25,000	8,80,000	Stock	1,03,000
General Reserve		1,88,000	Debtors	1,56,000
Creditors		2,16,000	Bank FD	2,25,000
			Bank balance	13,000
		12,84,000		12,84,000

Anuj decided to retire with effect from 1.4.2014.

The remaining partners agreed to share profits and losses equally in future.

The following adjustments were agreed to be made upon retirement of Anuj.

(i) Goodwill was to be valued at 1 year purchase of the average profits of the preceding 3 years on the date of retirement.

The average profits of the past 3 years were as follows:

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Year ended	₹	
31.3.2014	3,30,000	(as per draft accounts)
31.3.2013	2,32,000	
31.3.2012	2,20,900	

The partners decided not to raise goodwill account in the books.

(ii) The assets were revalued as follows:

Plant to be depreciated by 10%

Creditors amounting to ₹ 10,000 were omitted to be recorded;

₹ 6,000 is to be written off from stock;

Provision for doubtful debts to be created @ 5% of the debtors;

Interest accrued on FD amounting to ₹ 9,000 was omitted to be recorded.

The above adjustments were to be made from the profit for the year ended 31.3.2014 before calculation of goodwill.

(iii) Anuj agreed to take over the bank FD including interest accrued thereon in part payment of his dues and the balance would remain as a loan, carrying interest of 8% p.a.

(iv) Ayush and Piyush agreed to bring in sufficient cash to make their capital proportionate and maintain a bank balance of ₹ 1,50,000.

You are required to prepare

(I) Capital accounts of partners as on 1.4.2014 giving effect to the above adjustments.

(2) Balance Sheet as on 1.4.2014 after Anuj's retirement.

Accounting in Computerized Environment

16. What are the advantages of customized accounting packages?

Applicability of Accounting Standards

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

AS 1 "Disclosure of Accounting Policies

18. (a) Jagannath Ltd. had made a rights issue of shares in 2014. In the offer document to its members, it had projected a surplus of ₹ 40 crores during the accounting year to end on 31st March, 2015. The draft results for the year, prepared on the hitherto

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followed accounting policies and presented for perusal of the board of directors showed a deficit of ₹ 10 crores. The board in consultation with the managing director, decided on the following:

(i) Value year-end inventory at works cost (₹ 50 crores) instead of the hitherto method of valuation of inventory at prime cost (₹ 30 crores).

(ii) Provide depreciation for the year on straight line basis on account of substantial additions in gross block during the year, instead of on the reducing balance method, which was hitherto adopted. As a consequence, the charge for depreciation at ₹ 27 crores is lower than the amount of ₹ 45 crores which would have been provided had the old method been followed, by ₹ 18 cores.

(iii) Provide for permanent fall in the value of investments - which fall had taken place over the past five years - the provision being ₹ 10 crores.

As chief accountant of the company, you are asked by the managing director to draft the notes on accounts for inclusion in the annual report for 2014-2015.

AS 2 "Valuation of Inventories"

(b) CC Ltd., a Pharmaceutical Company, while valuing its finished stock at the year end wants to include interest on Bank Overdraft as an element of cost, for the reason that overdraft has been taken specifically for the purpose of financing current assets like inventory and for meeting day to day working expenses". State your comments on this treatment.

AS 6 "Depreciation Accounting"

19. (a) ABC Ltd. Purchased machine on 1-4-2011 for ₹ 2,00,000. The company charged depreciation at 10% on reducing balance method upto 2013-14. From 2014-15, the company decided to change depreciation method on straight line basis with estimated working life of 10 years and scrap value of ₹ 50,000. Compute the amount of depreciation to the charged to Profit and Loss Account for the year 2014-15.

AS 7 "Construction Contracts

(b) A contractor entered into a contract for building roads for ₹ 2 crores. After completing 60% of the contract he came to know that the cost of completing the contract would be ₹ 2.40 crores. The accountant transferred ₹ 0.24 crores i.e., 60% of total loss of ₹ 0.40 crores to Profit and Loss account in the current year. You are required to give your opinion in line with AS 7.

AS-10 "Fixed assets"

20. (a) Fire Ltd. purchased equipment for its power plant from Urja Ltd. during the year 2013-14 at a cost of ₹ 100 lacs. Fire Ltd. they paid only 90% and balance 10% was to be paid after one year on satisfactory performance of the equipment. During the

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Financial year 2014-15, Urja Ltd. waived off the balance 10% amount which was credited to Profit and Loss account by Fire Ltd. as discount received. Is this accounting treatment correct? State in line with Accounting Standards.

AS 13 "Accounting for Investment"

(b) M/s. Naren Garments Company Limited invested in the shares of another company on 1st November, 2014 at a cost of ₹ 3,00,000. It also earlier purchased Gold of ₹ 3,50,000 and Silver of ₹1,50,000 on 1st April, 2014. Market value as on 31st March, 2015 of the above investments is as follows:

	₹
Shares	2,50,000
Gold	5,00,000
Silver	2,80,000

How the above investments will be shown in the books of accounts of M/s Naren Garments Company Limited for the year ending 31st March, 2015 as per the provisions of AS-13 Accounting for Investments"?

SUGGESTED ANSWERS / HINTS

1. **Alpha Ltd.**

Balance Sheet as on 31st March, 2015

		Particulars	*Notes*	₹
		Equity and Liabilities		
1		Shareholders' funds		
	a	Share capital	1	49,95,000
	b	Reserves and Surplus	2	11,82,907
2		Non-current liabilities		
		Long-term borrowings	3	13,17,500
3		Current liabilities		
	a	Trade Payables		8,00,000
	b	Other current liabilities	4	37,500
	c	Short-term provisions	5	9,40,593
	d	Short-term borrowings		2,00,000
		Total		94,73,500

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		Assets		
1		Non-current assets		
		Fixed assets		
		Tangible assets	6	56,25,000
2		Current assets		
	a	Inventories	7	12,50,000
	b	Trade receivables	8	10,00,000
	c	Cash and cash equivalents	9	13,85,000
	d	Short-term loans and advances		2,13,500
		Total		94,73,500

Notes to accounts

			₹
1	Share Capital		
	Equity share capital		
	Issued & subscribed & called up		
	50,000 Equity Shares of ₹ 100 each		
	(of the above 10,000 shares have been issued for consideration other than cash)	50,00,000	
	Less: Calls in arrears	(5,000)	49,95,000
	Total		49,95,000
2	Reserves and Surplus		
	General Reserve	10,50,000	
	Add: current year transfer	20,000	10,70,000
	Profit & Loss balance		
	Profit for the year	4,33,500	
	Less: Appropriations:		
	Transfer to General reserve	(20,000)	
	Proposed Dividend (Refer W N)	(2,49,750)	
	DDT on Proposed dividend (Refer W N)	(50,843)	1,12,907
	Total		11,82,907
3	Long-term borrowings		
	Secured Term Loan		

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	State Financial Corporation Loan (7,50,000-37,500) (Secured by hypothecation of Plant and Machinery)		7,12,500
	Unsecured Loan		6,05,000
	Total		13,17,500
4	**Other current liabilities**		
	Interest accrued but not due on loans (SFC)		37,500
5	**Short-term provisions**		
	Provision for taxation	6,40,000	
	Proposed Dividend (Refer W N)	2,49,750	
	DDT on Proposed dividend (Refer W N)	50,843	9,40,593
6	**Tangible assets**		
	Land and Building	30,00,000	
	Less: Depreciation	(2,50,000)	27,50,000
	Plant & Machinery	35,00,000	
	Less: Depreciation	(8,75,000)	26,25,000
	Furniture & Fittings	3,12,500	
	Less: Depreciation	(62,500)	2,50,000
	Total		56,25,000
7	**Inventories**		
	Raw Materials		2,50,000
	Finished goods		10,00,000
	Total		12,50,000
8	**Trade receivables**		
	Outstanding for a period exceeding six months		2,60,000
	Other Amounts		7,40,000
	Total		10,00,000
9	**Cash and cash equivalents**		
	Cash at bank		
	with Scheduled Banks	12,25,000	
	with others (Omega Bank Ltd.)	10,000	12,35,000
	Cash in hand		1,50,000
	Total		13,85,000

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Working Note:

Calculation of grossing-up of dividend

Particulars	₹
Dividend distributed by Alpha Ltd. (5% of 49,95,000)	2,49,750
Add: Increase for the purpose of grossing up of dividend $\left[\frac{15}{100-15}\times 2,49,750\right]$	44,074
Gross dividend	2,93,824
Dividend distribution tax @ 17.304%	50,843

2. Cash Flow Statement as per AS 3

Cash flows from operating activities:		₹ *in lacs*
Net profit before tax provision		36,000
Add: Non cash expenditures:		
Depreciation	24,000	
Loss on sale of assets	48	
Interest expenditure (non operating activity)	12,000	36,048
		72,048
Less: Non cash income		
Amortisation of capital grant received	(10)	
Profit on sale of investments (non operating income)	(120)	
Interest income from investments (non operating income)	(3,000)	3,130
Operating profit		68,918
Less: Increase in working capital		(67,290)
Cash from operations		1,628
Less: Income tax paid		(5,100)
Net cash generated from operating activities		(3,472)
Cash flows from investing activities:		
Sale of assets (222 – 48)	174	
Sale of investments (33,318+120)	33,438	
Interest income from investments	3,000	
Purchase of fixed assets	(22,092)	

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Expenditure on construction work	(41,688)	
Net cash used in investing activities		(27,168)
Cash flows from financing activities:		
Grants for capital projects	18	
Long term borrowings	55,866	
Interest paid	(13,042)	
Dividend paid	(10,202)	
Net cash from financing activities		32,640
Net increase in cash		2,000
Add: Cash and bank balance as on 1.4.2014		6,000
Cash and bank balance as on 31.3.2015		8,000

3 Statement showing calculation of profits for pre and post incorporation periods for the year ended 31.3.15 (15 Months)

	Total (₹)	*Ratio*	*Pre* (₹)	*Post* (₹)
Gross profit	1,40,40,000	1:8	15,60,000	1,24,80,000
Less: Salaries	23,40,000	1:12	1,80,000	21,60,000
Depreciation	3,60,000	1:4	72,000	2,88,000
Advertisement	14,04,000	1:8	1,56,000	12,48,000
Discount	23,40,000	1:8	2,60,000	20,80,000
Managing director's remuneration	1,80,000	Post	-	1,80,000
Office cum showroom rent	14,40,000	Actual	1,80,000	12,60,000
Miscellaneous office expenses	2,40,000	1:4	48,000	1,92,000
Interest	19,02,000	Actual	7,02,000	12,00,000
Goodwill (bal. fig.)			38,000	--
Net profit (B.f.)			--	38,72,000

Note: Since the profits prior to incorporation are in the negative, they would be treated as goodwill.

Working Notes:

(1)	Calculation of Time Ratio	
	Pre-Incorporation Period	Post-Incorporation Period
	1st January, 2014 to 31st March, 2014	1st April, 2014 to 31st March, 2015

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	(3 Months)	(12 Months)
	3:	12
	1:	4
(2)	**Calculation of Sales Ratio**	
	Pre-Incorporation Period	Post-Incorporation Period
	3 Months	12 Months
	3 x 1	12 x 2
	3:	24
	1:	8
(3)	**Calculation of Staff Salary Ratio**	
	Pre-Incorporation Period	Post-Incorporation Period
	3 Months	12 Months
	3 x 1	12 x 3
	3:	36
	1:	12
(4)	**Calculation of Interest**	
	Pre-Incorporation Period	Post-Incorporation Period
	2,34,00,000 x 3/12 x 12/100	1,00,00,000 x 12/100
	= ₹ 7,02,000	= ₹ 12,00,000

(5) **Calculation of Rent**

Rent on additional space

1 July 2014 to 31st March, 2015	=	9 Months		
Total additional rent	=	60,000 x 9 = ₹ 5,40,000		
Remaining rent on earlier space	=	14,40,000 – 5,40,000 = ₹ 9,00,000		
Rent per month	=	$\frac{9,00,000}{15}$	=	₹ 60,000 per month
Pre-Incorporation Period rent	=	60,000 x 3	=	1,80,000
Post-Incorporation Period rent	=	60,000 x 12	=	7,20,000
Additional rent			=	5,40,000
				12,60,000

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(6) Calculation of Gross Profit

Trading Account

	₹		₹
To Cost of goods sold	3,27,60,000	By Sales	4,68,00,000
To Gross profit (Bal. fig.)	1,40,40,000		
	4,68,00,000		4,68,00,000

Note:

1. Pre incorporation period is 3 months upto 31st March 2014 and post incorporation period is of 12 months
2. As advertisement cost and discounts are directly related to sales, it is proper to assume that they would be incurred in the same ratio of time as Sales. Hence, 1 : 8
3 Since Managing Director is a position which is appointed in a company, it is proper to consider that his pay is incurred during the post incorporation period.
4. Interest on money borrowed to pay the purchase consideration is a post incorporation cost whereas the interest on purchase consideration for 3 months till payment will be pre incorporation cost.

4. Journal Entries in the books of Saral Ltd.

Capital Redemption Reserve A/c	Dr.	30,000	
Securities Premium A/c	Dr.	40,000	
Capital Reserve (Realized in cash*)	Dr	40,000	
General Reserve A/c	Dr.	40,000	
To Bonus to Shareholders			1,50,000
(Being issue of bonus shares by utilization of various Reserves, as per resolution dated …….)			
Bonus to Shareholders A/c	Dr.	1,50,000	
To Equity Share Capital			1,50,000
(Being capitalization of Profit)			

* Capital reserve amounting ₹ 40,000 realised in cash can only be used for bonus issue.

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5. Journal Entries

			₹ *in lacs*
		Dr.	*Cr.*
Equity Share Capital (₹ 10 each) A/c	Dr.	500	
To Equity Share Capital (₹ 2.50 each) A/c			125
To Capital Reduction A/c			375
(Conversion of all the equity shares into the same number of fully paid equity shares of ₹ 2.50 each as per scheme of Reconstruction)			
Director's Remuneration Outstanding A/c	Dr.	10	
To Capital Reduction A/c			10
(Outstanding remuneration foregone by the directors as per scheme of Reconstruction)			
12% Debentures A/c	Dr.	400	
Debenture Interest Outstanding A/c	Dr.	48	
To 13% Debentures A/c			400
To Capital Reduction A/c			48
(Conversion of 12% debentures into 13% debentures, Debenture holders forgoing outstanding debenture interest)			
Bank A/c	Dr.	125	
To Equity Share Application A/c			125
(Application money received for fully paid equity shares of ₹ 2.5 each from existing shareholders)			
Equity Share Application A/c	Dr.	125	
To Equity Share Capital (₹ 2.50 each) A/c			125
(Application money transferred to share capital)			
Trade payables A/c	Dr.	165	
To Equity Share Capital (₹ 2.50 each) A/c			65
To Bank A/c			80
To Capital Reduction A/c			20
(Trade payables for ₹ 65 lakhs accepting shares for full amount and those for ₹ 100 lakhs accepting cash equal to 80% of claim in full settlement)			

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Land and Building A/c	Dr.	46	
To Capital Reduction A/c			46
(Appreciation made in the value of land and building as per scheme of reconstruction)			
Capital Reduction A/c	Dr.	505	
To Goodwill A/c			15
To Plant and Machinery A/c			66
To Inventory A/c			22
To Trade receivables A/c			4
To Discount on issue of Debentures A/c			8
To Profit and Loss A/c			390
(Writing off losses and reduction in the values of assets as per scheme of reconstruction—W.N. 1)			
Capital Reserve A/c	Dr.	6	
To Capital Reduction A/c			6
(Being the loss on reconstruction (balance in the Capital Reduction A/c) transferred to Capital Reserve)			

Note: In a scheme of Capital Reduction, Goodwill, Losses etc should be written off against the Capital Reduction Account whether or not it is mentioned in the question.

Balance Sheet of Rocky Ltd. (and Reduced) as on 31st March, 2015

Particulars	*Note No.*	*Amount*
		₹ in lacs
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	315
(2) Non-Current Liabilities		
(a) Long-term borrowings - 13% Debentures		400
(3) Current Liabilities		
(a) Other current liabilities		11
(b) Short-term provisions		33
Total		759

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II. Assets		
(1) Non-current assets		
(a) Fixed assets		
(i) Tangible assets	2	491
(ii) Intangible assets	3	0
(2) Current assets		
(a) Current investments		
(b) Inventories		120
(c) Trade receivables		76
(d) Cash and cash equivalents(W.N.2)		72
Total		759

Notes to Accounts

			₹ in lacs
1	Share Capital		
	Equity Share Capital (₹2.50 each)	125	
	Add: Fresh issue	125	
	Add: Equity shares issued to trade payables	65	
	1,26,000 Fully paid equity shares of ₹ 2.50 each		315
	(26,000 shares have been issued for consideration other than cash)		
2	Tangible assets		
	(a) Land and Building	184	
	Add: Amount of appreciation under scheme of reconstruction	46	230
	(b) Plant and Machinery	286	
	Less: Amount written off under scheme of reconstruction dated.	(66)	220
	(c) Furniture and Fixtures		41
			491
3	Intangible assets		
	Goodwill	15	
	Less: Amount written off under scheme of reconstruction	15	-

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Working Notes:

1. Capital Reduction Account (₹ in lacs)

		₹			₹
To	Goodwill	15	By	Equity Share Capital A/c	375
To	Plant and Machinery	66	By	Director's Remuneration Outstanding A/c	10
To	Inventory	22	By	Debenture Interest Outstanding A/c	48
To	Trade receivables	4	By	Trade payables	20
To	Discount on issue of Debentures	8	By	Capital Reserve (Balancing Figure)	6
			By	Land and Building	46
To	Profit and Loss A/c	390			
		505			505

2. Cash at bank as on 31st March, 2015 (after reconstruction)

	₹ in lacs
Cash at bank (before reconstruction)	27
Add: Proceeds from issue of equity shares	125
	152
Less: Payment made to trade payables (80% of ₹ 100 Lakhs)	(80)
	72

6. (i) Calculation of Purchase consideration (or basis for issue of shares of AB Ltd.)

	A Ltd.	*BLtd.*
Purchase Consideration:	₹	₹
Goodwill	1,40,000	40,000
Freehold property	3,00,000	2,40,000
Plant and Machinery	1,00,000	40,000
Motor vehicles	30,000	20,000
Inventory	2,30,000	1,80,000
Trade receivables	2,00,000	80,000
Cash at Bank	80,000	40,000
	10,80,000	6,40,000
Less: Liabilities:		
6% Debentures (1,20,000 x 105%)	-	(1,26,000)

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Trade payables	(2,10,000)	(1,30,000)
Net Assets taken over	8,70,000	3,84,000
To be satisfied by issue of shares of AB Ltd. @ ₹10 each	87,000	38,400

(ii) Balance Sheet AB Ltd. as at 1st April, 2015

		Particulars	*Note No*	*Amount*
				₹
		EQUITY AND LIABILITIES		
1		Shareholders' funds		
	(a)	Share capital	1	12,54,000
2		Non-current liabilities		
	(a)	Long-term borrowings	2	1,26,000
3		Current liabilities		
	(a)	Trade payables (2,10,000+1,30,000)		3,40,000
		Total		17,20,000
		ASSETS		
1		Non-current assets		
	(a)	Fixed assets		
	i	Tangible assets	3	7,30,000
	ii	Intangible assets	4	1,80,000
2		Current assets		
	(a)	Inventories (2,30,000+1,80,000)		4,10,000
	(b)	Trade receivables (2,00,000+80,000)		2,80,000
	(c)	Cash and cash equivalents (80,000+40,000)		1,20,000
		Total		17,20,000

Notes to accounts

		₹	₹
1.	Share Capital		
	Equity share capital		
	1,25,400 shares of ₹10 each	12,54,000	

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	(All the above shares are issued for consideration other than cash)		
2.	**Long-term borrowings**		
	Secured		
	10% Debentures	1,26,000	
3.	**Tangible assets**		
	Freehold property		
	A Ltd.	3,00,000	
	B Ltd.	2,40,000	5,40,000
	Plant and Machinery		
	A Ltd.	1,00,000	
	B Ltd.	40,000	1,40,000
	Motor vehicles A Ltd.		
	A Ltd.	30,000	
	B Ltd.	20,000	50,000
			7,30,000
4.	**Intangible assets**		
	Goodwill		
	A Ltd.	1,40,000	
	B Ltd.	40,000	1,80,000

(iii) Journal Entries

In the books of AB Ltd.

Particulars		*Amount* (₹)	*Amount*(₹)
Business purchase account	Dr.	12,54,000	
To Liquidator of A Ltd. account			8,70,000
To Liquidator of B Ltd. account			3,84,000
(Being the amount of purchase consideration payable to liquidator of A Ltd. and B Ltd. for assets taken over)			
Goodwill	Dr.	1,40,000	
Freehold property	Dr.	3,00,000	
Plant and Machinery	Dr.	1,00,000	

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Motor vehicles	Dr.	30,000	
Trade receivables	Dr.	2,00,000	
Inventory	Dr.	2,30,000	
Cash at Bank	Dr.	80,000	
To Trade payables			2,10,000
To Business purchase account			8,70,000
(Being assets and liabilities of A Ltd. taken over)			
Goodwill	Dr.	40,000	
Freehold property	Dr.	2,40,000	
Plant and Machinery	Dr.	40,000	
Motor vehicles	Dr.	20,000	
Trade receivables	Dr.	80,000	
Inventory	Dr.	1,80,000	
Cash at Bank	Dr.	40,000	
To Trade payables			1,30,000
To 6% Debentures of B Ltd.			1,26,000
To Business purchase account			3,84,000
(Being assets and liabilities of B Ltd. taken over)			
6% Debentures of B Ltd.	Dr.	1,26,000	
To 10% debentures			1,26,000
(Being issue of 10% debentures to debenture holders of B Ltd.			
Liquidator of the A Ltd. account	Dr.	8,70,000	
Liquidator of the B Ltd. account	Dr.	3,84,000	
To Equity share capital account			
(Being the allotment of equity shares of ₹ 10 each, as per the agreement for discharge of purchase consideration)			12,54,000

7. Calculation of number of days from the base date

Due date	*Amount (₹)*	*No. of days from 5.3.15*	*Product*
5.3.2015	5,000	0	0
7.4.2015	7,500	33	2,47,500

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17.7.2015	6,000	134	8,04,000
14.9.2015	8,000	193	15,44,000
	26,500		25,95,500

$$\text{Average due date} = \text{Base date} + \frac{\text{Sum of Product}}{\text{Sum of Amount}}$$

$$= 5.3.2015 + \frac{25,95,500}{26,500} = 98 \text{ days (round off)}$$

The date of the cheque will be 98 days from the base date i.e.11.6.2015. So on 11th June, 2015, all bills will be settled by a single cheque payment.

8. Laxman in Account Current with Ram as on 31st Oct, 2014

Dr. *Cr.*

		₹	Days	Product (₹)			₹	Days	Product (₹)
01.07.14	To Bal. b/d	750	123	92,250	20.08.14	By Sales Returns	200	72	14,400
15.8.14	To Sales	1,250	77	96,250	22.09.14	By Bank	800	39	31,200
31.10.14	To Interest	18.48			15.10.14	By Cash	500	16	8,000
						By Balance of Products			1,34,900
					31.10.14	By Bal. c/d	518.48		
		2018.48		1,88,500			2018.48		1,88,500

$$\text{Interest} = ₹\ 1,34,900 \times \frac{5}{100} \times \frac{1}{365} = ₹\ 18.48$$

9. In Sales Ledger

General Ledger Adjustment Account

Date	*Particulars*	₹	*Date*	*Particulars*	₹
1.4.2015	To Balance b/d	3,400	1.4.2015	By Balance b/d	2,46,200
1.4.2015 to 30.4.2015	To Sales ledger adjustment A/c:		1.4.2015 to 30.4.2015	By Sales ledger adjustment A/c:	
	Sales return	21,700		Sales	9,74,900
	Cash received	8,62,100		B/R dishonoured	3,500
	Discount allowed	39,200	30.4.2015	By Balance c/d	5,200

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	B/R received	51,200			
30.4.2015	To Balance c/d (Bal. fig.)	2,52,200			
		12,29,800			12,29,800

10. Mayur Club

(i) Income and Expenditure Account for the year ended 31.3.2015

Expenditure		₹	*Income*	₹
To Sports Material used			By Subscription (W.N.2)	9,90,000
Opening stock	73,500		By Interest on fixed deposit	45,000
Add: Purchases	3,04,500			
	3,78,000			
Less: Closing stock	78,000	3,00,000		
To Salaries		3,15,000		
To Rent	1,48,500			
Add: Outstanding (W.N.6)	13,500	1,62,000		
To Ground maintenance		22,120		
To Insurance	38,400			
Less: Unexpired on 31.3.15	9,600			
	28,800			
Add: Unexpired on 1.4.14	8,400	37,200		
To Stationery used				
Opening stock	1,500			
Add: Purchases	3,450			
	4,950			
Less: Closing Stock	3,150	1,800		
To Sundry expenses		5,880		
To Depreciation on				
Furniture	27,000			
Sports equipment	31,500	58,500		
To Excess of income over expenditure		1,32,500		
		10,35,000		10,35,000

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Balance Sheet as at 31st March, 2015

Liabilities		₹	*Assets*		₹
Capital fund:			Equipments: Opening balance	1,80,000	
Opening balance (W.N.1)	10,95,000		*Add*: Addition	60,000	
Add: Excess of				2,40,000	
income over expenditure	1,32,500	12,27,500	*Less:* Depreciation (W.N.5)	31,500	2,08,500
Rent outstanding (W.N.6)		13,500	Furniture:	2,70,000	
Subscription received in advance for 2015-16		4,500	*Less*: Depreciation	27,000	2,43,000
			Sports material		78,000
			Stock of stationery		3,150
			Fixed deposit in bank		
			(4,50,000 + 1,50,000)		6,00,000
			Subscription in arrears:		
			For 2013-14 (W.N.3)	4,500	
			For 2014-15 (W.N.4)	27,000	31,500
			Prepaid insurance (unexpired)		9,600
			Cash on hand		31,750
			Cash at bank		40,000
		12,45,500			12,45,500

Working Notes:

1. Balance Sheet as at 31.3.2014

Liabilities	₹	*Assets*	₹
Capital fund (Bal. fig.)	10,95,000	Sports equipment	1,80,000
		Furniture	2,70,000
		Sports materials	73,500
		Stock of stationery	1,500
		Fixed deposits in bank	4,50,000

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		Subscription in arrears	22,500
		Prepaid insurance (unexpired)	8,400
		Cash on hand	39,100
		Cash at bank	50,000
	10,95,000		10,95,000

		₹
2.	**Income on account of subscription**	
	220 members @ ₹ 4,500 each	9,90,000
3.	**Subscription still in arrears of 2013-2014**	
	Opening balance of subscription in arrears (as on 1.4.2014)	22,500
	Less: Arrears subscription of 2013-14 received during the year 2014-15	18,000
	Subscription of 2013-14 still in arrears as on 31.3.2015	4,500
4.	**Subscription in arrear on 31.3.2015**	
	Subscription for the year 2014-15	9,90,000
	Less: Subscription received for the year	9,63,000
	Subscription in arrears for 2014-15	27,000
5.	**Depreciation on sports equipment**	
	On ₹ 1,80,000 @ 15% for full year	27,000
	On ₹ 60,000 @ 15% for 6 months	4,500
	Total	31,500
6.	**Outstanding rent of 2014-2015**	
	Outstanding rent = $\frac{₹\,1{,}48{,}500}{11\text{ months}} \times 1$ month	13,500

11. In the Books of Moonlight Traders

Trading Account for the year ended 31.03.2014

	Particulars	₹		*Particulars*	₹
To	Opening Stock A/c (Bal. fig.)	1,65,000	By	Sales (W.N.1)	12,50,000
To	Purchases (W.N.2)	9,00,000	By	Closing Stock	65,000
To	Gross profit (12,50,000x25/125)	2,50,000			
		13,15,000			13,15,000

Profit and Loss Account for the year ended 31.03.2014

	Particulars		₹		*Particulars*	₹
To	Discount		5,500	By	Gross profit	2,50,000
To	Salaries Expenses	32,000		By	Discount	4,500
To	Office expenses (W.N.3)	37,000				
To	Selling expenses	15,000	84,000			
To	Interest on loan (12% on ₹1,60,000)		19,200			
To	Bad debts (2% of ₹2,25,000)		4,500			
To	Loss on sale of Machinery		15,000			
To	Depreciation:					
	Land & Building	25,000				
	Plant & Machinery(W.N 4b)	23,750				
	Office Equipment (W.N. 5)	12,750	61,500			
To	Net profit after tax		64,800			
			2,54,500			2,54,500

Balance sheet as on 31.3.2014

Liabilities	₹	₹	*Assets*	₹
Capital (W.N. 6)	8,95,500		Land and Building (5,00,000-25,000)	4,75,000
Add: Net Profit	64,800	9,60,300	Plant and Machinery (W.N.4a) (3,30,000-21,750)	3,08,250
Creditors for Purchases (W.N. 8)		1,05,500	Office Equipment (85,000-12,750)	72,250
Outstanding expenses		15,000	Debtors less Bad debts (W.N. 7)	2,20,500
Loan from SBI		1,00,000	Stock	65,000
			Bank Balance (W.N. 9)	39,800
		11,80,800		11,80,800

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Working Notes:

1. Calculation of Total Sales

	₹
Cash Sales	2,50,000
Credit Sales (80% of total sales)	
Cash Sales (20% of total sales)	
Thus total Sales (250000 x 100/20)	12,50,000
Credit Sales (1250000 x 80/100)	10,00,000

2. Calculation of Total Purchases

	₹
Credit Purchases	5,40,000
Cash Purchases (40% of total purchases)	
Credit Purchases (60% of total purchases)	
Thus total Purchases (5,40,000 x 100/60)	9,00,000
Cash Purchases 9,00,000 x 40/100)	3,60,000

3. Office Expenses Account

	₹		₹
To Bank A/c	42,000	By Balance b/d	20,000
To Balance c/d	15,000	By Profit & loss A/c	37,000
	57,000		57,000

4. (a) Plant and Machinery Account

	₹		₹
To Opening balance	2,20,000	By Sale	40,000
To Purchases	1,50,000	By Closing Balance	3,30,000
	3,70,000		3,70,000

(b) Depreciation calculations on Plant & Machinery

		₹
Depreciation on	1,80,000 x 10% (for full year)	18,000
	1,50,000 x 10% x 3/12 (for 3 months)	3,750
	40,000 x 10% x 6/12 (for 6 months)	2,000
		23,750

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(c) Sale of Machinery Account

	Amount (₹)		*Amount* (₹)
To Plant & Machinery	40,000	By Depreciation	2,000
		By Profit and Loss a/c	15,000
		By Bank	23,000
	40,000		40,000

5. Depreciation calculations on Office Equipments

	₹
Opening Balance	1,05,000
Less: Closing Balance	85,000
Sale of Office Equipments	20,000
Balance of Office Equipments after sale	85,000
Depreciation @15%	12,750

6. Opening Balance Sheet as on 31.03.2013

	₹		₹
Creditors	95,000	Land & Building	5,00,000
Creditor for Exp.	20,000	Plant & Machinery	2,20,000
Loan	1,60,000	Office Equipment	1,05,000
Capital (Bal. fig.)	8,95,500	Debtors	1,55,500
		Stock	1,65,000
		Bank	25,000
	11,70,500		11,70,500

7. Sundry Debtors A/c

	₹		₹
To Balance b/d	1,55,500	By Bank	9,25,000
To Sales	10,00,000	By Discount	5,500
		By Bad debts	4,500
		By Bal. c/d	2,20,500
	11,55,500		11,55,500

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8. Sundry Creditors A/c

	₹		₹
To Bank	5,25,000	By Balance b/d	95,000
To Discount	4,500	By Purchases	5,40,000
To Balance c/d	1,05,500		
	6,35,000		6,35,000

9. Bank Account

	₹		₹
To Balance b/d	25,000	By Creditors	5,25,000
To Debtors	9,25,000	By Office Expenses	42,000
To Cash Sales	2,50,000	By Salary Expense	32,000
To Sale of Machinery (W.N. 4c)	23,000	By Selling Expenses	15,000
To Sale of equipment	20,000	By Purchases (cash)	3,60,000
		By Purchase of Machinery	1,50,000
		By Bank Loan & Interest.	79,200
		By Balance c/d	39,800
	12,43,000		12,43,000

12. Hire Purchase accounts in the buyer's books

(a) Tractors on Hire Purchase Account

2013				₹	*2013*				₹
April 1	To	HP Co. - Cash price			Dec. 31	By	Balance c/d		
		Tractor A		14,000			Tractor A	14,000	
Oct. 1	”	HP Co. - Cash price					Tractor B	19,000	33,000
		Tractor B		19,000					
				33,000					33,000
2014				₹	2014				₹
Jan. 1	To	Balance b/d			June 30	By	Disposal of Tractor A/c - Transfer		19,000
		Tractor A	14,000		Dec. 31	By	Balance c/d		14,000
		Tractor B	19,000	33,000					33,000
				33,000					
2015									
Jan. 1	To	Balance b/d		14,000					

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(b) Provision for Depreciation of Tractors Account

2013		₹	2013			₹
Dec. 31	To Balance c/d	3,050	Dec.31	By	P & L A/c:	
					Tractor A 2,100	
					Tractor B 950	3,050
		3,050				3,050
2014		₹	2014			₹
June30	To Disposal of Tractor account transfer	2,850	Jan. 1	By	Balance b/d	3,050
Dec. 31	To Balance c/d	4,900	Jun. 30	By	P & L A/c (Dep.) Tractor B	1,900
			Dec. 31		Tractor A	2,800
		7,750				7,750
			2013			₹
			Jan. 1	By	Balance b/d	4,900

(c) Disposal of Tractor Account

2014		₹	2014		₹
June30	To Tractors on hire purchase—Tractor B	19,000	June 30	By Provision for Depn. of Tractors A/c	2,850
			July 10	By Cash : Insurance	15,000
			Dec. 31	By P & L A/c : Loss	1,150
		19,000			19,000

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13. In the books of Smart Investments

12% Govt. Bonds for the year ended 31st March, 2014

Date	Particulars	Nos.	Income	Amount	Date	Particulars	Nos.	Income	Amount
1.4.13	To Opening balance b/d	1,200	3,600	1,26,000	30.6.13	By Bank A/c (Interest) (3,200 x 100 x 12% x 6/12)	-	19,200	-
2.5.13	To Bank A/c	2,000	8,000	1,92,000	30.9.13	By Bank A/c	1,500	4,500	1,57,500
31.3.14	To P & L A/c (Interest)		27,400		31.12.13	By Bank A/c (Interest) (1,700 x 100 x 12% x 6/12)	-	10,200	-
	To P & L A/c (Profit on Sale)			8,437.50	31.3.14	By Bal. c/d	1,700	5,100	1,68,937.50
		3,200	39,000	3,26,437.50			3,200	39,000	3,26,437.50

Investments in Equity shares of X Ltd. for year ended 31.3.2014

Date	Particulars	Nos.	Income	Amount	Date	Particulars	Nos.	Income	Amount
15.4.13	To Bank A/c	5,000		10,10,000					
3.6.13	To Bonus Issue	2,000	-	-	16.9.13	By Bank (Dividend)	-	-	7,500
31.8.13	To Bank A/c	800		2,00,000	15.12.13	By Bank (Sale)	3,000	-	8,91,000
31.3.14	To P & L A/c		4,800	4,28,500	15.1.14	By Bank (interim dividend)		4,800	
					31.3.14	By Bal. c/d	4,800		7,40,000
		7,800	4,800	16,38,500			7,800	4,800	16,38,500

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Working Notes:

1. Profit on sale of bonds on 30.9.13

   = Sales proceeds – Average cost

   Sales proceeds = ₹ 1,57,500

   Average cost = ₹ [(1,26,000+1,92,000) × 1,500/3,200] = 1,49,062.50

   Profit = 1,57,500– ₹ 1,49,062.50=₹ 8,437.50

2. Valuation of bonds on 31st March, 2014

   Cost = ₹ 3,18,000/3,200 x1,700 = 1,68,937.50

3. Cost of equity shares purchased on 15/4/2013

   = Cost + Brokerage

   = (5,000 ×₹ 200) + 1% of (5,000 × ₹ 200) = ₹ 10,10,000

4. Sale proceeds of equity shares on 15/12/2013

   = Sale price – Brokerage

   = (3,000 ×₹ 300) – 1% of (3,000 × ₹ 300) = ₹ 8,91,000.

5. Profit on sale of shares on 15/12/2013

   = Sales proceeds – Average cost

   Sales proceeds = ₹ 8,91,000

   Average cost = ₹ [(10,10,000+2,00,000-7,500) × 3,000/7,800]

   = ₹ [12,02,500 × 3,000/7,800] = 4,62,500

   Profit = ₹ 8,91,000 – ₹ 4,62,500=₹ 4,28,500.

6. Valuation of equity shares on 31st March, 2014

   Cost =₹ [12,02,500 × 4,800/7,800] = ₹ 7,40,000

   Market Value = 4,800 shares ×₹ 220 =₹ 10,56,000

   Closing stock of equity shares has been valued at ₹ 7,40,000 i.e. cost being lower than the market value.

Note: If rights are not subscribed for but are sold in the market, the sale proceeds are taken to the profit and loss statement as per para 13 of AS 13 "Accounting for Investments"

14. In the books of Mr. Black

Trading Account for the year ended 31.3.2014

	₹		₹
To Opening Stock	1,35,000	By Sales	9,00,000

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To Purchases	6,45,000	By Closing Stock at cost $\left(1{,}62{,}000\times\frac{100}{90}\right)$	1,80,000
To Gross Profit	3,00,000		
	10,80,000		10,80,000

Memorandum Trading A/c
for the period from 1.4.2014 to 02.06.2014

	₹		₹
To Opening Stock at cost	1,80,000	By Sales 4,80,000	
To Purchases 2,25,000 *Add:* Goods received but invoice not received 30,000 2,55,000		*Less:* Goods not dispatched 75,000	4,05,000
Less: Machinery 15,000	2,40,000	By Closing stock (Balancing figure)	1,50,000
To Gross Profit (Refer W.N.)	1,35,000		
	5,55,000		5,55,000

Calculation of Insurance Claim

Claim subject to average clause = $\left(\frac{\text{Actual loss of stock}}{\text{Value of stock on the date of fire}}\times\text{Amount of policy}\right)$

$$= 1{,}20{,}000 \text{ x } \left(\frac{1{,}50{,}000}{1{,}50{,}000}\right) = ₹\ 1{,}20{,}000$$

Working Note:

G.P. ratio = $\frac{3{,}00{,}000}{9{,}00{,}000}\times 100 = 33\frac{1}{3}\%$

Amount of Gross Profit = ₹ 4,05,000 x $33\frac{1}{3}\%$ = ₹ 1,35,000

15. Partners' Capital Accounts as on 1.4.2014

	Anuj	*Ayush*	*Piyush*		*Anuj*	*Ayush*	*Piyush*
To Anuj		22,950	68,850	By Balance b/d	3,75,000	2,80,000	2,25,000
To Revaluation Loss	37,400	37,400	18,700	By General Reserves	75,200	75,200	37,600
To Bank FD To 8% Loan	2,34,000 2,70,600			By Ayush and Piyush	91,800		
To Balance c/d*		3,03,450	3,03,450	By Cash (Bal. fig.)	-	8,600	1,28,400
	5,42,000	3,63,800	3,91,000		5,42,000	3,63,800	3,91,000

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Balance Sheet as on 1.4.2014 after Anuj's retirement

Liabilities	*Amount (₹)*	*Assets*	*Amount (₹)*
Anuj's Loan	2,70,600	Plant(90% of ₹ 7,87,000)	7,08,300
Creditors(2,16,000+10,000)	2,26,000	Stock (₹ 1,03,000 less ₹ 6,000)	97,000
Capital Accounts*:		Debtors(95% of ₹ 1,56,000)	1,48,200
Ayush	3,03,450	Bank Balance	1,50,000
Piyush	3,03,450		
	11,03,500		11,03,500

**Total of capital balances should be ₹ 6,06,900 which is proportioned to individual partners in their profit sharing ratio.*

Working Notes:

1. Profit / Loss on revaluation

Revaluation Account

	Amount (₹)		*Amount (₹)*
To Plant	78,700	By Interest on FD	9,000
To Creditors	10,000	By Loss on revaluation	93,500
To Inventory	6,000		
To Provision for doubtful debts	7,800		-
	1,02,500		1,02,500

2. Calculation of Goodwill

Goodwill Valuation

Profit of year ended	₹
31.3.2014 (₹ 3,30,000 less ₹ 93,500)	2,36,500
31.3.2013	2,32,000
31.3.2012	2,20,000
Total Profits	6,88,500

Average Profit = 6,88,500/3 = 2,29,500

Goodwill valued at 1 year purchase amounting ₹ 2,29,500.

3. Adjustment for goodwill among partners

Anuj's share of goodwill (2,29,500 x 2/5) = 91,800

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Gaining ratio of Ayush and Piyush

Ayush	Piyush
$\frac{1}{2}-\frac{2}{5}$	$\frac{1}{2}-\frac{1}{5}$
$\frac{5-4}{10}=\frac{1}{10}$	$\frac{5-2}{10}=\frac{3}{10}$

Gaining Ratio = 1: 3

Entry for adjustment of goodwill

		₹	₹
Ayush's capital A/c	Dr.	22,950	
Piyush's capital A/c	Dr.	68,850	
To Anuj's capital A/c			91,800
(Being Anuj's share of goodwill debited to remaining partners in their gaining ratio)			

16. Following are the advantages of the customized accounting packages:

    1. The input screens can be tailor made to match the input documents for ease of data entry.

    2. The reports can be prepared as per the specification of the organization. Many additional MIS reports can be included in the list of reports.

    3. Bar-code scanners can be used as input devices suitable for the specific needs of an individual organization.

    4. The system can suitably match with the organizational structure of the company.

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

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

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

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

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

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

18. (a) As per AS 1, any change in the accounting policies which has a material effect in the current period or which is reasonably expected to have a material effect in later periods should be disclosed. In the case of a change in accounting policies which has a material effect in the current period, the amount by which any item in the financial statements is affected by such change should also be disclosed to the extent ascertainable. Where such amount is not ascertainable, wholly or in part, the fact should be indicated. Accordingly, the notes on accounts should properly disclose the change and its effect.

Notes on Accounts:

(i) During the year inventory has been valued at factory cost, against the practice of valuing it at prime cost as was the practice till last year. This has been done to take cognizance of the more capital intensive method of production on account of heavy capital expenditure during the year. As a result of this change, the year-end inventory has been valued at ₹ 50 crores and the profit for the year is increased by ₹ 20 crores.

(ii) In view of the heavy capital intensive method of production introduced during the year, the company has decided to change the method of providing depreciation from reducing balance method to straight line method. As a result of this change, depreciation has been provided at ₹ 27 crores which is lower than the charge which would have been made had the old method and the old rates been applied, by ₹ 18 crores. To that extent, the profit for the year is increased.

(iii) The company has decided to provide ₹ 10 crores for the permanent fall in the value of investments which has taken place over the period of past five years. The provision so made has reduced the profit disclosed in the accounts by ₹ 10 crores.

(b) As per Accounting Standard 2 “Valuation of Inventories”, cost of inventories comprises all costs of purchase, costs of conversion and other costs incurred in bringing the inventories to their present location and condition. However, it makes clear that interest and other borrowing costs are usually not included in the cost of inventories because generally such costs are not related in bringing the inventories

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to their present location and condition. Therefore, the proposal of CC Ltd. to include interest on bank overdraft as an element of cost is not acceptable because it does not form part of cost of production.

19. (a) Depreciation charged by the company on reducing Balance method (from 2011-12) to 2013-14

Year	*Cost/WDV at the beginning of the year*	*Depreciation*		*WDV at the end of the year*
2011-12	2,00,000	2,00,000 x 10%	20,000	1,80,000
2012-13	1,80,000	1,80,000 x 10%	18,000	1,62,000
2013-14	1,62,000	1,62,000 x 10%	16,200	1,45,800

Depreciation charged on Straight Line Method (from 2011-12 to 2013-14)

$$= \frac{\text{Cost price of the machine - scrap value}}{\text{Useful life of machine}}$$

$$= \frac{₹\ 2,00,000 - ₹\ 50,000}{10} = 15,000$$

Book Value of machine at the end of 2013-14 by Straight Line Method (SLM)

= ₹ 2,00,000 – [15,000 + 15,000 + 15,000] = ₹1,55,000

Depreciation to be charged in 2014-15

Particulars	₹
Book value of the machine as per Reducing Balance Method as on 2013-14	1,45,800
Less: Book value of the machine as per Straight Line Method as on 2013-14	(1,55,000)
Difference of Depreciation	(9,200)
Add: Depreciation for the year 2014-15 as per Straight Line Method	15,000
Depreciation charged to Profit and Loss Account in the year 2014-15	5,800

(b) As per AS 7, when it is probable that total contract costs will exceed total contract revenue, the expected loss should be recognized as an expense immediately irrespective of the stage of completion.

In the given case the revenue that can be recognized for the contract i.e. ₹ 2 crore and the expected expense on the contract is ₹ 2.4 cores. 60% of the contract has been completed. Therefore as per AS 7 whole amount of expected loss i.e. ₹ 0.40 crores should be recognized as an expense immediately irrespective of the stage of completion of the contract. Therefore the action of accountant of transferring only ₹ 0.24 crores to the profit & loss a/c is wrong. He must transfer whole ₹ 0.40 crore to profit & loss a/c as an expense.

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20. (a) According to AS 10 on Accounting for Fixed Assets, the cost of an asset may undergo changes subsequent to its acquisition on account of exchange fluctuation, price adjustment, changes in duty or similar factors. Such changes in price/cost needs to be adjusted with the cost of the asset.

In the give case, Fire Ltd., initially accounted for 100% amount i.e., ₹ 100 lacs as cost of fixed asset although they paid only ₹ 90 lacs and kept ₹ 10 lacs as payable to the credit of Urja Ltd. Now since the supplier has waived off the balance amount of ₹ 10 lacs, this should be treated as change in price and needs to be adjusted with the cost of asset as per AS 10.Therefore, the treatment given by Fire Ltd., in crediting ₹ 10 lacs as discount to Profit & Loss Account is completely wrong and needs to be corrected.

(b) As per AS 13 "Accounting for Investments", for Investments in shares – If the Investment is purchased with an intention to hold for short – term period then it will be shown at the realizable value of ₹ 2,50,000 as on 31st March, 2015.

If equity shares are acquired with an intention to hold for long-term period 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, if other than temporary, in the value of Investments.

As per the Standard, investment acquired for long term period shall be shown at cost. Gold and Silver are generally purchased with an intention to hold it for long term period until and otherwise given. Hence the investment in Gold and silver (purchases on 1st April 2014 shall continue to be shown at cost as on 31st March 2015 i.e. ₹ 3,50,000 and ₹1,50,000 respectively, though their realizable values have been increased. If held as short term then it should be valued at lower of cost or fair value (Market price)

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Applicability of Pronouncements/Legislative Amendments/Circulars etc. for November, 2015 – Intermediate (IPC) Examination

Paper 1: Accounting

Accounting Standards

AS	1	:	Disclosure of Accounting Policies
AS	2	:	Valuation of Inventories
AS	3	:	Cash Flow Statements
AS	6	:	Depreciation Accounting
AS	7	:	Construction Contracts (Revised 2002)
AS	9	:	Revenue Recognition
AS	10	:	Accounting for Fixed Assets
AS	13	:	Accounting for Investments
AS	14	:	Accounting for Amalgamations

Note Regarding Applicability for Paper 1 :

The relevant notified Sections of the Companies Act, 2013 up to 31st March, 2015 and for other legislative amendments including relevant Notifications / Circulars / Rules / Guidelines issued by Regulating Authority up to 30th April, 2015.

Non-Applicability of Ind ASs:

The Ministry of Corporate Affairs has notified Roadmap for applicability of Indian Accounting Standards (Ind AS) vide Notification No. G.S.R.......(E) dated 16 February, 2015, for compliance by the class of companies specified in the said roadmap. The notification has been uploaded on www.mca.gov.in along with the thirty nine (39) Indian Accounting Standards (Ind AS). **Students may note that these Ind ASs are not applicable for November, 2015 Examination.**

Paper 2: Business Laws, Ethics and Communication

The Companies Act, 2013 : The relevant sections of the Companies Act, 2013, notified up to 31st March, 2015 along with significant Rules/ Notifications/ Circulars/ Clarifications/ Orders issued by the Ministry of Corporate Affairs upto 30th April, 2015.

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PAPER – 2: BUSINESS LAWS, ETHICS & COMMUNICATION

PART – I: ANNOUNCEMENTS STATING APPLICABILITY & NON-APPLICABILITY FOR NOVEMBER, 2015 EXAMINATION

I. Applicability for November 2015 examinations

Applicability of relevant amendments/Circulars/Notifications/Regulations etc. for the period 1st May 2014 to 30th April, 2015 relating to Business Law, Ethics and Communication at Intermediate (IPC) for November 2015, Examination:

(i) The Companies Act, 2013

Sl. No.	Amendment related to the topic	Content
1.	Associate Company	Vide General Circular no. 24/2014 dated 25th of June 2014 Ministry of Corporate Affairs issued a clarification with regard to holding of shares in a fiduciary capacity by associate company under section 2(6) of the Companies Act, 2013.
2.	Delegation of power and functions to ROC under the sections related to the Memorandum, Companies with charitable objects,& Alteration of memorandum	As per the Notification S.O. 1353(E), dated 9th Of July, 2014 and in supersession of the notification of the Government of India, MCA, dated the 10.07.2012 vide no. S.O. 1538(E), dated 10.07.2012, Central Government hereby delegates to the ROC the power & functions vested in it under the following sections of the said Act- 4(2), 8, 13(2) which deals with the memorandum, Companies with charitable objects,& Alteration of memorandum respectively.
3.	Delegation of powers and functions to the Regional Director(RD) under the sections related to the Memorandum, Companies with charitable objects,& Alteration of	Vide Notification S.O. 1352(E) dated 21.05.2014 and in supersession of the notification of the Government of India, MCA, dated the 10.07.2012 the Central Govt. hereby delegates to the RD at Mumbai, Kolkata, Chennai, Noida, Ahmedabad, Hyderabad & Shillong, the power & functions vested in it under the following sections of the said Act, subject to the condition that the Central Govt.

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	memorandum, Rectification of name of company and Commencement of business.	may revoke such delegation of powers or may itself exercise the powers & functions under the sections, 8(6), 13(4) &(5), 16, 11(3) if in its opinion, such course of action is necessary in the public interest,: These sections deals with Memorandum, Companies with charitable objects,& Alteration of memorandum, Rectification of name of company and Commencement of business.
4.	Registration of names of the Companies	Vide General Circular No. 29/2014 dated 11th of July 2014 the Ministry of Corporate Affairs directed Registrar to ensure that registration of names of the Companies shall be in consonance with the provisions of the Emblems and Names (Prevention of Improper Use) Act, 1950.
5.	Registration of names of the Companies	General Circular No. 02/2014, dated 11.02.2014 was issued on the use of word 'National' and 'Bank' in the names of Companies or LLP.
6.	Private Placement	As per the Companies (Prospectus and Allotment of Securities) Amendment Rules, 2014, dated 30th June 2014 further a new proviso has been added with respect to an offer or invitation for non-convertible debentures It says that when an offer or invitation for non-convertible debentures is made within a period of six months from the date of commencement of these rules, the special resolution may be passed within the said period of six months from the date of commencement of these rules.
8.	Acceptance of deposits from public	As per the Companies (Removal of Difficulties) Second Order, 2014 dated 2nd of June, 2014 and the Companies (Removal of Difficulties) Fourth Order, 2014 dated 6th of June 2014, the Central Government hereby makes the order that

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		until a date is notified by the Central Government, the Company Law Board shall exercise the jurisdiction, powers, authority and functions of the Tribunal.
9.	Further issue of Capital	As per the Companies (Share Capital and Debenture) Amendment Rules, 2014, dated 18th of June, 2014, after Sub-Rule (2) of rule 13 related to issue of shares on preferential basis, following sub-rule (3) has been inserted stating that the price of shares or other securities to be issued on preferential basis shall not be less than the price determined on the basis of valuation report of a registered valuer.
10.	Debenture	Conditions for the issue of secured debentures by a company prescribed under the Companies (Share Capital and Debentures) Rules, 2014. According to which issue of secured debentures may be made, provided the date of its redemption shall not exceed ten years from the date of issue And also inclusion of amendment as per the Companies (Share Capital and Debentures) Amendment Rules, 2014 .According to which classes of companies that may issue secured debentures for a period exceeding ten years but not exceeding thirty years.
11.	Debenture redemption reserve (DRR) account	After the "RBI (Amendment) Act, 1997" the following is inserted "and for Housing Finance Companies registered with the National Housing Bank" as per the Companies (Share Capital and Debentures) Amendment Rules, 2014
12.	Voting through electronic means	Clarifications on issues associated with e-voting procedure issued by the Ministry of Corporate Affairs vide General Circular No. 20/2014 dated 17th June 2014 for clarity and ensuring uniformity

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		in the e-voting procedure.
13.	Declaration in respect of beneficial interest in any share	A proviso has been inserted under Rule 9 sub rule 3 by the Companies (Management and Administration) Second Amendment Rules, 2014 with respect to section 89 of the Companies Act, 2013. "Provided that nothing contained in this rule with respect to section 89 of the Companies Act, 2013 shall apply in relation to a trust which is created, to set up a Mutual Fund or Venture Capital Fund or such other fund as may be approved by the Securities and Exchange Board of India".
14.	Annual return	As per the Companies (Management and Administration) Second Amendment Rules, 2014 a changes have been carried out in the Companies (Management and Administration) Amendment Rules, 2014 in Rule 13 whereby the words “either value or volume of the shares" is omitted along with the explanation giving meaning of ‘change’.
15.	Voting and right to demand a poll	Vide Notification dated 19th March, 2015, Central Government further amended the Companies(Management and Administration) Rules, 2014 by issuing the Companies (Management and Administration) Amendment Rules, 2015 whereby replacing the rule 20 of the Companies (Management and Administration) Rules, 2014 relating to the Voting through electronic means.
16.	Place of keeping and inspection of registers, returns, etc	Vide Notification dated 31st March, 2015, the Central Government hereby delegates to the Regional Directors at Mumbai, Kolkata, Chennai, Noida, Ahmedabad, Hyderabad and Shillong, the powers and functions vested in it under sub-section (5) of section 94 of the Companies Act,2013.

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(ii) The Employees' Provident Funds & Miscellaneous Provisions Act, 1952

Revised statutory wage ceiling from ₹ 6500/- to ₹ 15,000 per month under the Employees Provident Funds (Amendment) Scheme, 2014, Employees Pension (Amendment) Scheme 2014 and the Employees Deposit Linked Insurance (Amendment) Scheme, 2014.

Students are advised to refer the study material (July 2014 edition) along with the practice manual (December 2014 edition).

II. Non-Applicability for November 2015 examinations

(i) The following sections of the Companies Act, 2013 are not applicable for November 2015 examinations: Section 48 relating to "Variation of shareholders' right", Section 66 related to "Reduction of share capital", Section 75 relating to 'damages for fraud', Section 97 relating to "Power of tribunal to call AGM", Section 98 relating to "Power of Tribunal to call meetings of members, etc., and Section 99 relating to "Punishment for default in complying with provisions of sections 96 to 98", of the Companies Act, 2013.

(ii) The Companies (Amendment) Act, 2015

PART – II : QUESTIONS AND ANSWERS

QUESTIONS

PART – A: BUSINESS LAWS

The Indian Contract Act, 1872

1. (a) Mr. David started "self service" system in his shop. Ms. Marry entered the shop, took a basket and after taking articles of her choice into the basket reached the cashier for payments. The cashier refuses to accept the price. Can Mr. David be compelled to sell the said articles to Ms. Marry? Decide.

(b) Rishi proposed to sell his house to Rajan. Rajan sent his acceptance by post. Next day, Rajan sends a telegram withdrawing his acceptance. Examine the validity of the acceptance in the light of the following:

(i) The telegram of revocation of acceptance was received by Rishi before the letter of acceptance.

(ii) The telegram of revocation and letter of acceptance both reached together.

2. (a) Explain in brief the rules relating to 'Acceptance' of an offer under the provisions of the Indian Contract Act, 1872.

(b) A, the bailor, pledges a cinema projector and other accessories with Cine Association Co-operative Bank Limited, the bailee, for a loan. A requests the bank to allow the pledged goods to remain in his possession and promises to hold the

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same in trust for the bailee and also further promises to handover the possession of the same to the bank whenever demanded. Examining the provisions of the Indian Contract Act, 1872 decide, whether a valid contract of pledge has been made between A, the bailor and Bank, the bailee?

The Negotiable Instruments Act, 1881

3. (a) John, a shareholder of a Company purchased for his personal use certain goods from a Mall (Departmental Store) on credit. He sent a cheque drawn on the Company's account to the Mall (Departmental Store) towards the full payment of the bills. The cheque was dishonoured by the Company's Bank. John, the shareholder of the company was neither a Director nor a person in-charge of the company. Examining the provisions of the Negotiable Instruments Act, 1881 state whether John has committed an offence under Section 138 of the Act and decide whether he (John) can be held liable for the payment, for the goods purchased from the Mall (Departmental Store).

   (b) Mr. Big, a major, and Minion, a minor, executed a promissory note in favour of Ms. Purva. Examine with reference to the provisions of the Negotiable Instruments Act, the validity of the promissory note and whether it is binding on Mr. Big and Minion.

4. 'P' draws a cheque for ₹ 50,000. When the cheque ought to be presented to the drawee bank, the drawer has sufficient funds to make payment of the cheque. The bank fails before the cheque is presented. The payee demands payment from the drawer. What is the liability of the drawer.

The Payment of Bonus Act, 1965

5. Peter is working as a salesman in a company on salary basis. The following payments were made to him by the company during the previous financial year–

   (i) overtime allowance,

   (ii) dearness allowance

   (iii) commission on sales

   (iv) employer's contribution towards pension fund

   (v) value of food.

   Examine as to which of the above payments form part of "salary" of Peter under the provisions of the Payment of Bonus Act, 1965.

6. Achal limited company earned super profits during financial year. It intends to give maximum bonus to its employees. In this regard you are asked to advice the company on permissible maximum bonus under the Payment of Bonus Act, 1965.

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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. Satish retired from the services of Life Management Limited, on 31st March, 2014. He had a sum of ₹ 5 lac in his Provident Fund Account. It has become due for payment to Satish on 30th April, 2014 but the company made the payment of the said amount after one year. Satish claimed for the payment of interest on due amount at the rate of 15 percent per-annum for one year. Decide, whether the claim of Satish is tenable under the provisions of the Employees' Provident Funds and Miscellaneous Provisions Act, 1952.

The Payment of Gratuity Act, 1972

9. When an employee becomes disabled due to any accident or disease and is unable to do the same work and re-employed on the reduced wages, how the gratuity of such employee shall be, computed under the provisions of the Payment of Gratuity Act, 1972?

10. Elle was an employee of Tea Estate Ltd. The whole of the undertaking of Tea Estate Ltd. was taken over by a new company - Asia Tea Estate Ltd. The services of Elle remained continuous in new company. After serving for one year Elle met with an accident and became permanently disabled. Elle applied to the new company for the payment of gratuity. The company refused to pay gratuity on the ground that Elle has served only for a year in the company.

    Examine the validity of the refusal of the company in the light of the provisions of the Payment of Gratuity Act, 1972.

The Companies Act, 2013

11. An association of 120 persons has been formed with the object of acquisition of gain. Now, due to an internal mismanagement, the said association has applied for being wound up under the provisions of the Companies Act, 2013. Advice.

12. XYZ Co. Ltd. was in the process of incorporation. Promoters of the company signed an agreement for the purchase of certain furniture for the company and payment was to be made to the suppliers of furniture by the company after incorporation. The company was incorporated and the furniture was used by it. Shortly after incorporation, the company went into liquidation and the debt could not be paid by the company for the purchase of above furniture. As a result suppliers sued the promoters of the company for the recovery of money.

    Examine whether promoters can he held liable for payment under the following situations:

    (i) When the company has already adopted the contract after incorporation?

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(ii) When the company makes a fresh contract with the suppliers in terms of pre incorporation contract?

13. Explain the meaning of ordinary and special resolutions as discussed under the Companies Act, 2013.

14. Write a note on 'Report on Annual General Meeting' under the Companies Act, 2013.

15. 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.

PART – B: ETHICS

16. Explain the meaning of the terms 'ethics' and 'business ethics'. What kind of awareness is required for being ethical in business.

17. State the elements which create discrimination in employment in the business organizations.

18. State in brief the guidelines for managing ethics and to prevent the need for whistle-blowing in the work place.

19. (i) What is meant by 'Environmental ethics'? How does its non-adoption lead to 3 Ps Viz., Polluter Pays and Principles? Explain.

    (ii) Explain the reasons for unethical behaviour among finance and accounting professionals.

20. Examine the following hypothetical situation and give a brief analytical note on it.

    Kalam Ltd. has been the leading scientific equipment manufacturing company in South India. But it suddenly finds that certain companies from North India that do not have anywhere near its own kind of clout in their own turfs, are trying to enter the south Indian market. But because of its superior clout, Kalam Ltd coerces them to enter into agreement with itself such that they do not sell at prices above that of its own products. Please comment on the legality of such agreements. Conversely, if Kalam Ltd were to enter into agreements with distributors such that the distributors are prevented from marketing the products of the North Indian companies, would that be illegal?

PART – C: COMMUNICATION

21. "Importance of communication is increasing day-by-day in the business organizations". State the reasons for this increasing importance.

22. Explain the functions of interpersonal communication.

23. Explain Consensus Building.

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24. Mr. Atul has not received a dividend warrant of ₹ 1,500 for 150 shares of Xtra Ltd. Draft an indemnity bond, to be given to the company for seeing release of Dividend.

25. Draft a business letter, presuming your facts that you have received the goods from the company and you are sending payments.

SUGGESTED ANSWERS/HINTS

1. (a) **Invitation to offer** : The offer should be distinguished from an invitation to offer. An offer is the final expression of willingness by the offeror to be bound by his offer should the party chooses to accept it. Where a party, without expressing his final willingness, proposes certain terms on which he is willing to negotiate, he does not make an offer, but invites only the other party to make an offer on those terms. This is the basic distinction between offer and invitation to offer.

The display of articles with a price in a self-service shop is merely an invitation to offer. It is in no sense an offer for sale, the acceptance of which constitutes a contract. In this case, Ms. Marry by selecting some articles and approaching the cashier for payment simply made an offer to buy the articles selected by her. If the cashier does not accept the price, the interested buyer cannot compel him to sell. [*Fisher V. Bell (1961) Q.B. 394 Pharmaceutical society of Great Britain V. Boots Cash Chemists].*

(b) The problem is related with the communication and time of acceptance and its revocation. As per Section 4 of the Indian Contract Act, 1872, the communication of an acceptance is a complete as against the acceptor when it comes to the knowledge of the proposer.

An acceptance may be revoked at any time before the communication of the acceptance is complete as against the acceptor, but not afterwards.

Referring to the above provisions

(i) Yes, the revocation of acceptance by Rajan (the acceptor) is valid.

(ii) If Rishi opens the telegram first (and this would be normally so in case of a rational person) and reads it, the acceptance stands revoked. If he opens the letter first and reads it, revocation of acceptance is not possible as the contract has already been concluded.

2. (a) Following are the general rules regarding acceptance under the Indian Contract Act, 1872.

(i) Acceptance must be absolute and unqualified. As per section 7 of the Act, acceptance is valid only when it is absolute and unqualified or unconditional.

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(ii) Acceptance must be in the prescribed manner. If the offer is not accepted in the prescribed manner, then the offeror may reject the acceptance within a reasonable time.

(iii) Acceptance must be communicated to the offeror. If acceptance is communicated to the person, other than the offeror, it will not create any legal relationship. Thus, to conclude a contract between the parties, the acceptance must be communicated in some perceptible form.

(iv) Acceptance must be given by the party to whom the offer is made.

(v) Acceptance must be given within the prescribed time or within a reasonable time.

(vi) Acceptance cannot be given before communication of an offer

(vii) Acceptance must be made before the offer lapses or is withdrawn.

(viii) Acceptance must show intention to fulfill the promise.

(ix) Acceptance cannot be presumed from silence

(x) Acceptance by conduct/performance of condition: Acceptance may also be by performance of some condition / act as required by the Offer or.

(b) Delivery to pawnee under Indian Contract Act, 1872: The problem as asked in the question is based on the provisions of the Indian Contract Act, 1872 as contained in Section 149 (delivery to bailee and pledgee). The Section provides that the delivery of the goods to the bailee may be made by actual or constructive delivery or delivery by attornment to the bank. In such a case there is change in the legal character of the possession of goods though not in the actual or physical custody. Though the bailor continues to be in possession of the goods, it is the possession of the bailee.

In the given problem the delivery of the goods is constructive i.e. delivery by attornment to the bailee (pawnee) and the possession of the goods by A, the bailor is construed as possession by bailee/pawnee, the Bank. A constructive pledge comes into existence as soon as the pawnor, without actually delivering the goods, promises to deliver them on demand. The transaction was, therefore, a valid pledge. On this point, the decision given by the Andhra Pradesh High Court in *Bank of Chittur Ltd. vs. Narasimhulu AIR 1966 AP 163* is relevant.

3. (a) The facts of the problem are identical with the facts of a case known as *H.N.D. Mulla Feroze Vs. C.Y. Somaya Julu, J(2004) 55 SCL (AP)* wherein the Andhra Pradesh High Court held that although the petitioner has a legal liability to refund the amount to the appellant, petitioner is not the drawer of the cheque, which was dishonoured and the cheque was also not drawn on an account maintained by him but was drawn on an account maintained by the company. Hence, it was held that the petitioner John could not be said to have committed the offence under Section

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138 of the Negotiable Instruments Act, 1881. Therefore is not liable for the cheque but legally liable for the payments for the goods.

(b) **Minor being a party to negotiable instrument:** According to section 26 of the Negotiable Instruments Act, 1881, every person competent to contract has capacity to incur liability by making, drawing, accepting, endorsing, delivering and negotiating a promissory note, bill of exchange or cheque.

As a minor's agreement is void, he cannot bind himself by becoming a party to a negotiable instrument. But he may draw, endorse, deliver and negotiate such instruments so as to bind all parties except himself.

In view of the provisions of Section 26 explained above, the promissory note executed by Mr. Big and Minion is valid even though a minor is a party to it. Minion, being a minor is not liable; but his immunity from liability does not absolve the other joint promisor, namely Mr. Big from liability *[Sulochana v. Pandiyan Bank Ltd., AIR (1975) Mad. 70].*

4. Section 84 of the Negotiable Instruments Act, 1881 provides that where a cheque is not presented for payment within a reasonable time of its issue and the drawer or person on whose account it is drawn had the right at the time when presentation ought to have been made, as between himself and the banker, to have the cheque paid and suffers actual damage through the delay, he is discharged from the liability, that is to say, to the extent to which such drawer or person is a creditor of the banker to a larger amount than would have been if such cheque had been paid. In determining what is a reasonable time, regard shall be had to the nature of the instrument, the usage of trade and of banker, and the facts of the particular case.

Applying the above provisions to the given problem since the payee has not presented the cheque to the drawer's bank within a reasonable time when the drawer had funds to pay the cheque, and the drawer has suffered actual damage, the drawer is discharged from the liability.

5. **Computation of Salary / Wages:** According to Section 2(21) of the Payment of Bonus Act, 1965 salary and wages means all remuneration other than remuneration in respect of overtime work, capable of being expressed in terms of money, which would if the terms of employment, express or implied, were fulfilled, be payable to an employee in respect of his employment, or of work done in such employment and includes dearness allowance, i.e. all cash payment by whatever name called, paid to an employee on account of a rise in the cost of living. But the term excludes:

(i) Any other allowance which the employee is for the time being entitled to;

(ii) The value of any house accommodation or of supply of light, water, medical attendance or other amenities of any service or of any concessional supply of food grains or other articles;

(iii) Any traveling concession;

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(iv) Any bonus including incentive, production or attendance bonus;

(v) Any contribution paid or payable by the employer to any pension fund or for benefit of the employee under any law for the time being in force.

(vi) Any retrenchment compensation or any gratuity or other retirement benefit payable to the employee or any ex-gratia payment made to him; and

(vii) Any commission payable to the employee.

It has been clarified in the explanation to the section that where an employee is given, in lieu of the whole or part of the salary or wage payable to him, free food allowance or free food by his employer, such food allowance or the value of such food shall be deemed to form part of the salary or wage for such employee.

In view of the provisions of Section 2(21) explained above, the payment of dearness allowance and value of free food by the employer forms part of salary of Peter while remaining three payments i.e. payment for overtime, commission on sales and employer's contribution towards pension funds shall not form part of his salary.

6. Where, in respect of any accounting year referred to in Section 10 of the Payment of Bonus Act,1965, the allocable surplus exceeds the amount of minimum bonus payable to the employees under that section, the employer shall, in lieu of such minimum bonus, be bound to pay to every employee in respect of that accounting year bonus which shall be an amount in proportion to the salary or wage earned by the employee during the accounting year subject to a maximum 20% of such salary or wage.

   In the given case therefore, the company will be free to give bonus at any rate exceeding 8.33% upto a maximum of 20% of the salary or wage earned by the employees during the accounting year. From the facts given, it may be presumed that the bonus at 20% may be payable.

   However, in relation to the maximum bonus payable the most important term to understand is "allocable surplus". The eligibility for maximum bonus arises from the "allocable surplus" but is not limited by it, as the allocable surplus may justify a bonus at a rate higher than 20% but bonus will still be limited to 20%.

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

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

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

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

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

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

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

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

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

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

9. **Computation of Gratuity of a disabled employee:** According to Section 4 (4) of the Payment of Gratuity Act, 1972, when an employee becomes disabled due to any accident or disease and is not in a position to do the same work and re-employed on reduced wages on some other job, the gratuity will be calculated in two parts :-

   - For the period preceding the disablement: on the basis of wages last drawn by the employee at the time of his disablement.
   - For the period subsequent to the disablement: On the basis of the reduced wages as drawn by him at the time of the termination of services.

   In the case of *Bharat Commerce and Industries Vs. Ram Prasad,* it was decided that if for the purposes of computation of quantum of the amount of gratuity the terms of agreement or settlement are better than the Act, the employee is entitled for that benefit.

   However, the maximum statutory ceiling limit as providing under Sub-Section 3 of Section 4 of the Act (the maximum amount of gratuity payable to an employee shall not exceed ₹ 10 lakh), cannot be reduced by mutual settlement or agreement.

10. According to Section 4 (1) of the Payment of Gratuity Act, 1972, gratuity shall be payable to an employee on the termination of his employment after he has rendered continuous

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service for not less than five years on his superannuation, or, on his retirement or resignation or on his death or disablement due to accident or disease.

The proviso to the subsection states that the condition of the completion of five years of continuous service is not essential in case of the termination of the employment of any employee due to death or disablement for the purpose of this section.

Disablement has been explained as such disablement which incapacitates an employee for the work which he was capable of performing before the accident or disease resulting in such disablement.

The given problem fulfils all the above requirements as stated. Therefore, Elle is entitled to recover gratuity after becoming permanently disabled and continuous service of five years is not required in this case. Hence, the company cannot refuse to pay gratuity on the ground that he has served only for a year.

11. According to section 464 of the Companies Act, 2013, no association or partnership consisting of more than prescribed number of persons shall be formed for the purpose of carrying on any business that has for its object the acquisition of gain by the association or partnership or by the individual members thereof, unless it is registered as a company under the Companies Act or is formed under any other law for the time being in force. Further, the prescribed number of persons shall not exceed 100.

    The association as mentioned in the question exceed the prescribed number of members i.e., it consists of 120 members. Where an association is formed, which has membership in excess of the number aforementioned, will be an illegal association. Such a body will have no legal existence and it cannot be wound up under the Act, or even as an unregistered company. Neither a member of it would be able to sue it, nor would it be able to sue the member.

    Further, every member of an association or partnership carrying on business in contravention of above law, shall be punishable with fine which may extend to one lakh rupees and shall also be personally liable for all liabilities incurred in such business.

12. The present contract has been entered into by the promoters for purchase of furniture. The terms of the contract provide for the payment by the XYZ Co Ltd after it is incorporated. A pre incorporation contract is not binding on the company as it was not in existence on the date of the contract. Such a contract can also not be entered into by promoters acting as agents of the company as the company not being in existence cannot appoint agents.

    Therefore, the contract for the purchase of furniture cannot be binding on the company.

    The promoters remain personally liable on a contract made on behalf of a company which is not yet in existence. Such a contract is deemed to have been entered into personally by the promoters and they are liable to pay damages for failure to perform the promises made in the company's name *(Scot v. Lord Ebury)*, even though the contract expressly provided that only the company shall be answerable for performance.

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In *Kelner v. Baxter* also it was held that the persons signing the contracts viz. Promoters were personally liable for the contract.

Further, a company cannot ratify a contract entered into by the promoters on its behalf before its incorporation. Therefore, it cannot by adoption or ratification obtain the benefit of the contract purported to have been made on its behalf before it came into existence as ratification by the company when formed is legally impossible. The doctrine of ratification applies only if an agent contracts for a principal who is in existence and who is competent to contract at the time of contract by the agent.

The company can, if it desires, enter into a new contract, after its incorporation with the other party. The contract may be on the same basis and terms as given in the pre-incorporation contract made by the promoters. The adoption of the pre-incorporation contract by the company will not create a contract between the company and the other parties even though the option of the contract is made as one of the objects of the company in its Memorandum of Association. It is, therefore, safer for the promoters acting on behalf of the company about to be formed to provide in the contract that: (a) if the company makes a fresh contract in terms of the pre-incorporation contract, the liability of the promoters shall come to an end; and (b) if the company does not make a fresh contract within a limited time, either of the parties may rescind the contract.

Thus applying the above principles, the answers can be as under:

(i) the promoters in the first case will be liable to the suppliers of furniture. There was no fresh contract entered into with the suppliers by the company. Therefore, promoters continue to be held personally liable in this case for the reasons given above.

(ii) in the second case obviously the liability of promoters comes to an end provided the fresh contract was entered into on the same terms as that of pre-incorporation contract.

13. (1) Ordinary resolution: A resolution shall be an ordinary resolution if the notice required under this Act has been duly given and it is required to be passed by the votes cast, whether on a show of hands, or electronically or on a poll, as the case may be, in favour of the resolution, including the casting vote, if any, of the Chairman, by members who, being entitled so to do, vote in person, or where proxies are allowed, by proxy or by postal ballot, exceed the votes, if any, cast against the resolution by members, so entitled and voting.

(2) Special resolution: A resolution shall be a special resolution when—

(a) the intention to propose the resolution as a special resolution has been duly specified in the notice calling the general meeting or other intimation given to the members of the resolution;

(b) the notice required under this Act has been duly given; and

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(c) the votes cast in favour of the resolution, whether on a show of hands, or electronically or on a poll, as the case may be, by members who, being entitled so to do, vote in person or by proxy or by postal ballot, are required to be not less than three times the number of the votes, if any, cast against the resolution by members so entitled and voting.

14. Section 121 of the Companies Act, 2013 provides the preparation of report on each Annual General Meeting which is to be filed with the registrar. The section says that-

(1) Report to be prepared by the listed public company: Every listed public company shall prepare in the prescribed manner a report on each annual general meeting including the confirmation to the effect that the meeting was convened, held and conducted as per the provisions of this Act and the rules made thereunder.

(2) Filing of the report with the registrar: The company shall file with the Registrar a copy of the report within thirty days of the conclusion of the Annual General Meeting with such fees as may be prescribed, or with such additional fees as may be prescribed, within the time as specified, under section 403.

(3) Default in filing of the report: If the company fails to file the report before the expiry of the period specified under section 403 with additional fee, the company shall be punishable with fine which shall not be less than one lakh rupees but which may extend to five lakh rupees and every officer of the company who is in default shall be punishable with fine which shall not be less than twenty-five thousand rupees but which may extend to one lakh rupees.

The rules provided on the Report on Annual General Meeting given under the Companies(Management and administration) rules, 2014 says that-

(I) The report shall be prepared in the following manner, namely:-

(a) the report under this section shall be prepared in addition to the minutes of the general meeting;

(b) the report shall be signed and dated by the Chairman of the meeting or in case of his inability to sign, by any two directors of the company, one of whom shall be the Managing director, if there is one and company secretary of the company;

(c) the report shall contain the details in respect of the following, namely:-

(i) the day, date, hour and venue of the annual general meeting;

(ii) confirmation with respect to appointment of Chairman of the meeting;

(iii) number of members attending the meeting;

(iv) confirmation of quorum;

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(v) confirmation with respect to compliance of the Act and the Rules, secretarial standards made there under with respect to calling, convening and conducting the meeting;

(vi) business transacted at the meeting and result thereof;

(vii) particulars with respect to any adjournment, postponement of meeting, change in venue; and

(viii) any other points relevant for inclusion in the report.

(d) the Report shall contain fair and correct summary of the proceedings of the meeting.

(II) The copy of the report as prepared above, shall be filed with the Registrar in prescribed Form within thirty days of the conclusion of the Annual General Meeting along with the fee.

15. Yes, the Director shall be held liable for the false statements in the prospectus under sections 34 and 35 of the Companies Act, 2013. Section 34 imposes a criminal punishment on every person who authorises the issue of such prospectus Whereas section 35 more particularly includes a director of the company in the imposition of civil liability for such mis-statements.

The only situations when a director will not incur any liability for mis-statements in a prospectus are as under:

(a) No criminal liability under section 34 shall apply to a person if he proves that such statement or omission was immaterial or that he 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.

(b) No civil liability for any mis-statement under section 35 shall apply to a person if he proves that:

(i) Having consented to become a director of the company, he withdrew his consent before the issue of the prospectus, and that it was issued without his authority or consent; or

(ii) The prospectus was issued without his knowledge or consent, and that on becoming aware of its issue, he forthwith gave a reasonable public notice that it was issued without his knowledge or consent.

Therefore, in the present case the director cannot hide behind the excuse that he had relied on the promoters for making correct statements in the prospectus. He will be liable for mis-statements in the prospectus.

16. 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.

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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.

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.

17. The root meaning of the term discriminate is "to distinguish one object from another " Employment discrimination is treating one person better than another because of their age, gender, race, religion or other protected class of status. Discrimination in employment is wrong because it violates the basic principle of equality. Discrimination is to treat people differently. It is usually intended to refer to the wrongful act of making a difference in treatment or favour on a basis other than individual merit.

Elements of Discrimination: Generally, the discrimination means to distinguish one object from another or treating people differently. It is usually intended to refer to the wrongful act of making a difference in treatment or favour on a basis other than individual merit. Such discrimination may also be related in employment in business organization. The elements which create discrimination may be summarized as follows:

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

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

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

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

18. Managing ethics and preventing whistle-blowing: The focus on core values and sound ethics, the hall mark of ethical management, is being recognized as an important way to ensure the long term effectiveness of governance structures and procedures and to avoid the need for whistle blowing.

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Employers, who understand the importance of work place ethics, provide their work force with an effective framework and guiding principles of identity and address ethical issues as they arise. These guidelines for managing ethics and to avoid the need for whistle-blowing in the work place may be summarized as follows:-

(a) Have a Code of Conduct and ethics.

(b) Establishment open communication.

(c) Make ethical decisions in group and make decision public whenever appropriate.

(d) Integrate ethics with other management practices.

(e) Use of cross functional teams when developing and implementing the ethics management programme.

(f) Appointing an ombudsman.

(g) Creating an atmosphere of trust.

(h) Regularly updating of policies and procedures

(i) Include a grievance policy for employees

(j) Set an example from the top.

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

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

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

(ii) The reasons which lead to unethical behaviour among finance and accounting professionals are as follows:

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1. **Emphasis on short term results :** This is one of the primary reasons which has led to the downfall of many companies like Enron and Worldcom.
2. **Ignoring small unethical issues:** It is a known fact that most of the compromises we make are small, however, they lead us into committing large infractions. Ignoring minor lapses, lead to bigger and huge mistakes.
3. **Economic cycles:** In good times, companies are relaxed in their accounting procedures or disclosures, as there is a pervasive feel-good effect. But when times of hardship follow, then the hit taken by them is almost fatal, as was proved in the Enron case. So companies need to watch out for economic cycles and be vigilant in good times as well as bad.
4. **Accounting rules:** In the era of globalization and massive cross border flow of capital, accounting rules are changing faster than ever before. The rules have become more complex and it is difficult to identify deviations from these complex set of requirements. The complexity of these principles and rules and the difficulty associated with identifying abuse are reasons which may promote unethical behaviour

20. The Competition Act, 2002 intends to provide, keeping in view of the economic development of the country, for the establishment of a Commission to prevent practices having adverse effect on competition, to promote and sustain competition in markets, to protect the interests of consumers and to ensure freedom of trade carried on by other participants in markets, in India, and for matters connected therewith or incidental thereto.

The Act deals with the following:

- **Prohibition of certain agreements**, which are considered to be anti-competitive in nature. Such agreements [namely tie in arrangements, exclusive dealings (supply and distribution), refusal to deal and resale price maintenance] shall be presumed as anti-competitive if they cause or are likely to cause an appreciable adverse effect on competition within India.
- **Abuse of dominant position** by imposing unfair or discriminatory conditions or limiting and restricting production of goods or services or indulging in practices resulting in denial of market access or through in any other mode are prohibited.
- **Regulation of combinations** which cause or likely to cause an appreciable adverse effect on competition within the relevant market in India.

In light of the above points, any agreement that Kalam Ltd. may enter into with its competitors from North India to tie-up the price at a certain level is prohibited. Such agreements would also amount to abuse of dominant position.

Conversely, agreements with distributors preventing the latter from distributing the goods of its competitors would also be illegal since they would restrict market access and can be deemed anti-competitive.

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21. Reasons for increasing importance of communication: It is true that importance of communication is increasing day by day in the business organizations. The reasons for this growth may be stated as follows:

    (a) Growth in the size and multiple locations of organization: Most of the organizations are growing larger and large in size. The people working in these organizations may be spread over different states of a country or over different countries. Keeping in touch, sending directions across and getting feedback is possible only when communication lines are kept working effectively.

    (b) Growth of trade unions: Over the last so many decades trade unions have been growing strong. No management can be successful without taking the trade unions in confidence. Only through effective communication can a meaningful relationship be built between the management and workers.

    (c) Growing importance of human relations: Workers in an organization are not like machines. They have their own hopes and aspirations. Management has to recognize them above all as sensitive human beings and work towards a spirit of integration with them which effective communication helps to achieve.

    (d) Public Relations: Every organization has a social responsibility, towards customers, government, suppliers and the public at large. Communication with them is the only way an organization can project a positive image of itself.

    (e) Advance in Behavioural Sciences: Modern management is deeply influenced by exciting discoveries made in behavioural sciences like psychology, sociology, transactional analysis etc. All of them throw light on subtle aspects of human nature and help in developing a positive attitude towards life and building up meaningful relationships. And this is possible only through communication.

    (f) Technological advancement: The world is changing very fast, owing to scientific and technological advancements. These advancements deeply affect not only methods of work but also the composition of groups. In such a situation proper communication between superiors and subordinates becomes very necessary.

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.

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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. Consensus Building: Consensus means overwhelming agreement. Most consensus building efforts set out to achieve unanimity. The key indicator of whether or not a consensus has been reached is that everyone agrees with the final proposal and it is important that consensus be the product of a good-faith effort to meet the interests of all stakeholders. Thus, consensus requires that someone frame a proposal after listening carefully to everyone's interests. Before the parties in a consensus building process come together, mediators (or facilitators) can play an important part in helping to identify the right participants, assist them in setting an agenda and clarifying the ground rules by which they will operate, and persuading noncompliant parties to participate. Once the process has begun, mediators (and facilitators) try to assist the parties in their efforts to generate a creative resolution of differences.

    ♦ Problem-Solving Orientation - It is important to be constructive and maintain a problem-solving orientation, even in the face of strong differences and personal antagonism. It is in every participant's best interest to behave in a fashion they would like others to follow. Concerns or disagreement should be expressed in an unconditionally constructive manner.

    ♦ Engage in Active Listening-Participants in every consensus building process should be encouraged (indeed, instructed, if necessary) to engage in what is known as active listening a procedure for checking to be sure that communications are being heard as intended.

    ♦ Disagree Without Being Disagreeable-Participants in every consensus building process should be instructed to "disagree without being disagreeable." This dictum should probably be included in the group's written ground rules.

    ♦ Strive for the Greatest Degree of Transparency Possible-To the greatest extent possible, consensus building processes should be transparent. That is, the group's mandate, its agenda and ground rules, the list of participants and the groups or interests they are representing, the proposals they are considering, the decision rules they have adopted, their finances, and their final report should, at an appropriate time, be open to scrutiny by anyone affected by the group's recommendations.

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♦ Strive to Invent Options for Mutual Gain-The goal of a consensus building process ought to be to create as much value as possible and to ensure that whatever value is created be divided in ways that take account of all relevant considerations. The key to creating value is to invent options for mutual gain.

24. Mr. Atul S/o ………………….. resident ………………… do hereby agree to indemnify the Xtra Ltd. for any loss that may occur for seeking release of dividend for 150 shares of ₹ 1500.

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

Mr. Atul

Date: Signature

Place:

25. Business Letter - acknowledging receipt of goods:

KUNAL CHEMICALS LIMITED

Regd. Office : 15, Okhla Estate, New Delhi - 110016

Phone : 6132757, Fax : 6132767

E-mail: kunalchem@rediffmail.com , website: www.kunalchem.org

Messrs. Shippers & Perfect Delivers Dated:

16, Nariman Point

Mumbai

Sir

Subject: Acknowledging the receipt of Consignment No ______

Reference: Our request 24/FD/55 – dated 1st August, 2015

We acknowledge with thanks the receipt of above consignment in our godown and we are arranging the payment of proceeds towards the said consignment by way of crossed cheque in favour of your company within a period of next 15 days.

We solicit your relationship in our future dealings.

Thanking you

Yours faithfully

For on behalf of Kunal Chemicals Ltd.

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Applicability of Pronouncements/Legislative Amendments/Circulars etc. for November, 2015 – Intermediate (IPC) Examination

Paper 1: Accounting

Accounting Standards

AS	1	:	Disclosure of Accounting Policies
AS	2	:	Valuation of Inventories
AS	3	:	Cash Flow Statements
AS	6	:	Depreciation Accounting
AS	7	:	Construction Contracts (Revised 2002)
AS	9	:	Revenue Recognition
AS	10	:	Accounting for Fixed Assets
AS	13	:	Accounting for Investments
AS	14	:	Accounting for Amalgamations

Note Regarding Applicability for Paper 1 :

The relevant notified Sections of the Companies Act, 2013 up to 31st March, 2015 and for other legislative amendments including relevant Notifications / Circulars / Rules / Guidelines issued by Regulating Authority up to 30th April, 2015.

Non-Applicability of Ind ASs:

The Ministry of Corporate Affairs has notified Roadmap for applicability of Indian Accounting Standards (Ind AS) vide Notification No. G.S.R.......(E) dated 16 February, 2015, for compliance by the class of companies specified in the said roadmap. The notification has been uploaded on www.mca.gov.in along with the thirty nine (39) Indian Accounting Standards (Ind AS). **Students may note that these Ind ASs are not applicable for November, 2015 Examination.**

Paper 2: Business Laws, Ethics and Communication

The Companies Act, 2013 : The relevant sections of the Companies Act, 2013, notified up to 31st March, 2015 along with significant Rules/ Notifications/ Circulars/ Clarifications/ Orders issued by the Ministry of Corporate Affairs upto 30th April, 2015.

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PAPER – 3: COST ACCOUNTING AND FINANCIAL MANAGEMENT

PART I: COST ACCOUNTING

QUESTIONS

Material

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

   For the month of November 2015, it has been anticipated that a demand for 60,000 packs of surgical gloves will arise. Aditya Brothers purchases these gloves from the manufacturer at ₹ 228 per pack within a 4 to 6 days lead time. The ordering and related cost is ₹ 240 per order. The storage cost is 10% p.a. of average inventory investment.

   Required:

   (i) Calculated the Economic Order Quantity (EOQ)

   (ii) Calculate the number of orders needed every year

   (iii) Calculate the total cost of ordering and storage of the surgical gloves.

   (iv) Determine when should the next order to be placed. (Assuming that the company does maintain a safety stock and that the present inventory level is 10,033 packs with a year of 360 working days).

Labour

2. Arnav Limited manufactures and sales plastic chairs. It pays wages under the differential piece rate system by following F.W. Taylor's System with a standard piece rate of ₹ 12.50 per unit of chair produced by the workers. Standard production per hour is 4 chairs. Each worker is supposed to work 8 hours a day from Monday to Friday and 5 hours on Saturday. Presently, there are 118 workers who are entitled for this plan.

   The plant and machinery used to manufacture the chairs was purchased long back and does not match with the efficiency of the workers. Workers appraised their concerns to the management and demanded wages on the time rate basis i.e. ₹ 50 per hour and the incentive under the Halsey Premium plan.

   The following production estimates has been made for the month of November, 2015 under the three scenarios:

Scenario	Worst case	Optimal case	Best case
Production (in units)	42,400	84,960	1,27,400

   Required:

   (a) Calculate total wages and average wages per worker per month, under the each scenario, when

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(i) Current system of wages and incentive payment system is followed

(ii) Workers' demand for time rate wages and Halsey premium plan is accepted.

(b) Mr. K, during the month of October 2015, has produced 1,050 units. What will be impact on his earning if he will be able to produce the same number of units in next month also. Should he support the workers' demand?

(Take 4 working weeks in a month)

Overheads

3. PQR manufacturers – a small scale enterprise, produces a single product and has adopted a policy to recover the production overheads of the factory by adopting a single blanket rate based on machine hours. The annual budgeted production overheads for the year 2015-16 are ₹ 44,00,000 and budgeted annual machine hours are 2,20,000.

For a period of first six months of the financial year 2015 -2016, following information were extracted from the books:

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

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

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

The actual machine hours worked during the period were 1,16,000 hours. It is revealed from the analysis of information that ¼ of the under/ over absorption was due to defective production policies and the balance was attributable to increase/decrease in costs.

Required:

(i) Determine the amount of under/over absorption of production overheads for the six months period of 2015-16.

(ii) Show the accounting treatment of under/ over absorption of production overheads, and

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(iii) Apportion the under/ over absorbed overheads over the items.

Non-integrated Accounting

4. As of 31st March, 2015, the following balances existed in a firm's cost ledger, which is maintained separately on a double entry basis:

	Debit(₹)	Credit(₹)
Stores Ledger Control A/c	3,20,000	–
Work-in-progress Control A/c	1,52,000	–
Finished Goods Control A/c	2,56,000	–
Manufacturing Overhead Control A/c	–	28,000
Cost Ledger Control A/c	–	7,00,000
	7,28,000	7,28,000

During the next quarter, the following items arose:

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

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

Contract Costing

5. Get – Homes Constructions has undertaken three separate building contracts. Information relating to these contracts for the year 2014-15 are as under:

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	Contract –I (Amount in ₹'000)	Contract –II (Amount in ₹'000)	Contract –IIII (Amount in ₹'000)
Value of contract	17,500	14,500	24,500
Balance as on 01-04-2014:			
Work completed and certified	--	4,100	8,150
Materials at site	--	220	310
Plant & Machinery (WDV)	--	770	3,760
Wages outstanding	--	48	104
Profit transferred to Costing P/L A/c.	--	--	350
Transaction during the year:			
Materials issued to the sites	870	2,150	4,020
Wages paid to workers	450	1,160	2,180
Salary to site staffs	90	85	135
Travelling and other expenses	18	24	32
Plants issued to sites	910	240	680
Apportionment of Head office expenses	110	90	126
Balance as on 31-03-2015:			
Materials at site	215	152	12
Plant & Machinery (WDV)	728	808	3,552
Wages outstanding	52	98	146
Value of work certified	2,000	8,600	24,000
Cost of work not certified	800	452	560

As per the contract agreement 15% of the certified value of the contract is kept by the contractees as retention money. The Contact-III is scheduled to be completed in the coming months, however, this contract required a further estimated cost of ₹ 7,20,000 to get it completed.

Required:

(a) Prepare Contract Statement for each of the three contracts and calculate the notional/ estimated profit/ loss

(b) Calculate the profit/ loss to be transferred to Costing Profit & Loss Account for internal managerial purpose.

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Process Costing

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

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

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

	(₹)
Raw Material	23
Labour	7
Overheads	9
	39

   Required:

   (a) Calculate the quantity (in litres) of raw material inputs during the month.

   (b) Calculate the quantity (in litres) of normal loss expected from the process and the quantity (in litres) of abnormal loss / gain experienced in the month.

   (c) Calculate the values of raw material, labour and overheads added to the process during the month.

   (d) Prepare the process account for the month.

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Standard Costing

7. Jigyasa Pharmaceuticals Ltd. is engaged in producing dietary supplement 'Funkids' for growing children. It produces 'Funkids' in a batch of 10 kgs. Standard material inputs required for 10 kgs. of 'Funkids' are as below:

Material	Quantity (in kgs.)	Rate per kg. (in ₹)
Vita-X	5	110
Proto-D	3	320
Mine-L	3	460

During the month of March, 2015, actual production was 5,000 kgs. of 'Funkids' for which the actual quantities of material used for a batch and the prices paid thereof are as under:

Material	Quantity (in kgs.)	Rate per kg. (in ₹)
Vita-X	6	115
Proto-D	2.5	330
Mine-L	2	405

You are required to calculate the following variances based on the above given information for the month of March, 2015 for Jigyasa Pharmaceuticals Ltd.:

(i) Material Cost Variance;

(ii) Material Price Variance;

(iii) Material Usage Variance;

(iv) Material Mix Variance;

(v) Material Yield Variance.

Marginal Costing

8. T Ltd produces a single product 'T-10' and sells it at a fixed price of ₹ 2,050 per unit. The production and sales data for first quarter of the year 2014-15 are as follows:

	April	May	June
Sales in units	4,200	4,500	5,200
Production in units	4,600	4,400	5,500

Actual/budget information for each month was as follows:

Direct materials	4 kilograms at ₹120 per kilogram
Direct labour	6 hours at ₹60 per hour

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Variable production overheads	150% of direct labour
Sales commission	15% of sales value
Fixed production overheads	₹ 5,00,000
Fixed selling overheads	₹ 95,000

There was no opening inventory at the start of the quarter. Fixed production overheads are budgeted at ₹ 60,00,000 per annum and are absorbed into products based on a budgeted normal output of 60,000 units per annum.

Required:

(a) Prepare a profit statement for each of the three months using absorption costing principles.

(b) Prepare a profit statement for each of the three months using marginal costing principles.

(c) Present a reconciliation of the profit or loss figures given in your answer to (a) and (b).

Budget and Budgetary Control

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

The following forecast information has been extracted from departmental estimates for the year ended 31st March 2016 (the budget period):

	Product M	Product N
Sales (units)	28,000	13,000
Finished goods stock increase by year-end	320	160
Post-production rejection rate (%)	4	6
Material Z usage (per completed unit, net of wastage)	5 kg	6 kg
Material Z wastage (%)	10	5

Additional information:

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

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Required:

(a) Prepare functional budgets for the year ended 31st March 2016 under the following headings:

(i) Production budget for Products M and N (in units).

(ii) Purchases budget for Material Z (in kgs and value).

(b) Calculate the Economic Order Quantity for Material Z (in kgs).

(c) If there is a sole supplier for the raw material Z in the market and the supplier do not sale more than 4,000 kg. of material Z at a time. Keeping the management purchase policy and production quantity mix into consideration, calculate the maximum number of units of Product M and N that could be produced.

Miscellaneous

10. (a) Define Product costs. Describe three different purposes for computing product costs.

(b) What do you understand by Operating Costs? Describe its essential features and state where it can be usefully implemented?

(c) How apportionment of joint costs upto the point of separation amongst the joint products using market value at the point of separation and net realizable value method is done? Discuss.

(d) Explain:

(i) Pre-production Costs

(ii) Research and Development Costs

(iii) Training Costs

SUGGESTED HINTS/ANSWERS

1. (i) Calculation of Economic Order Quantity:

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

= 3,893.3 packs or 3,893 packs.

(ii) Number of orders per year

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

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(iii) Ordering and storage costs

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

(iv) Timing of next order

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

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

supply.

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

(b) Days requirement covered by inventory

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

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

(c) Time interval for placing next order

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

5 days – 5 days = 0 days

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

2. (a) Calculation of Total wages and average wages per worker per month.

(i) When Current system of wages and incentive payment system is followed:

		Worst case	Optimal case	Best case
I	Standard Production (in units) (45 hours × 4 units × 4 weeks × 118 workers)	84,960	84,960	84,960
II	No. of units to be produced	42,400	84,960	1,27,400
III	Efficiency {(II ÷ I) × 100}	49.91%	100%	149.95%

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IV	Differential piece rate*	₹10 (₹12.5× 0.8)	₹15 (₹12.5 × 1.2)	₹15 (₹12.5 × 1.2)
V	Total Wages (II × IV)	₹4,24,000	₹12,74,400	₹19,11,000
VI	Average wages per worker (V ÷ 118)	₹3,593.22	₹10,800	₹16,194.92

*For efficiency less than 100%, 83% of piece rate and for efficiency more than or equals to 100%, 125% of piece rate may also be taken.

(ii) When workers' demand for time rate wages and Halsey premium plan is accepted:

		Worst case	Optimal case	Best case
I	No. of units expected to be produced (units)	42,400	84,960	1,27,400
II	Standard no. units in an hour (units)	4	4	4
III	Standard Hours (I ÷ II)	10,600	21,240	31,850
IV	Expected working hours (45 hours × 4 weeks × 118 workers)	21,240	21,240	21,240
V	Hours to be saved (III – IV)	--	--	10,610
VI	Time wages (IV × ₹50)	₹10,62,000	₹10,62,000	₹10,62,000
VII	Incentive under Halsey Premium Plan $\left(\frac{1}{2}\times \text{Time saved} \times ₹\ 50\right)$	--	--	₹2,65,250
VIII	Total Wages (VI +VII)	₹10,62,000	₹10,62,000	₹13,27,250
IX	Average wages per worker (VIII ÷ 118)	₹9,000	₹9,000	₹11,247.88

(b) Calculation of gain or loss in the current monthly income of Mr. K:

	Wages earned in October 2015:	
	Standard production unit (45 hours × 4 weeks × 4 units)	720 units
	No. of units produced	1,050 units
	Efficiency	145.83%
	Differential piece rate (refer the above part)	₹15
I	Total wages (1,050 units × ₹15)	₹15,750

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	Expected wages under the new scheme	
	Standard hours (1,050 units ÷ 4 units)	262.50 hours
	Expected hours to be taken (45 hours × 4 weeks)	180 hours
	Time saved	82.50 hours
	Time wages (180 hours × ₹50)	₹9,000
	Incentive $\left(\frac{1}{2} \times \text{Time saved} \times ₹50\right)$	₹2,062.50
II	Total expected wages	₹11,062.50
	Loss from the proposed scheme (II – I)	₹4,687.50

Supporting the demand of colleague workers will cost ₹4,687.50 in the next month to Mr. K.

3. (i) Amount of under/ over absorption of production overheads during the period of first six months of the year 2015-2016:

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

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

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

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Amount to be transferred to Costing Profit and Loss Account = (11,700 * ¼) ₹ 2,925

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

Amount to be distributed = (11,700 * ¾) ₹ 8,775

Supplementary rate = $\frac{₹\ 8,875}{33,000 \text{ units}}$ = ₹ 0.2689 per unit

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

	Equivalent completed units	Amount (₹)
Work-in-Progress (18,000 units × 50% × ₹ 0.2689)	9,000	2,420
Finished goods (2,400 units × ₹ 0.2689)	2,400	646
Cost of sales (21,600 units × ₹ 0.2689)	21,600	5,809
Total	33,000	8,875

4. Cost Ledger Control Account

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

Stores Ledger Control Account

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

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WIP Control Account

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

Finished Stock Ledger Control Account

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

Manufacturing Overhead Control Account

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

Wages Control Account

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

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Cost of Sales Account

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

Trial Balance

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

5. (a) Contract Statement (Amount in ₹'000)

	Contract-I (₹)	Contract-II (₹)	Contract-III (₹)
Balance as on 01-04-2014:			
- Work completed and certified	--	4,100	8,150
- Materials at site	--	220	310
- Plant & Machinery	--	770	3,760
Transaction during the year:			
Materials issued	870	2,150	4,020
Wages paid to workers	450	1,160	2,180
Less: Outstanding at beginning	--	(48)	(104)
Add: Outstanding at closing	52	98	146
Salary to site staffs	90	85	135
Travelling and other expenses	18	24	32
Plant issued to sites	910	240	680
Apportionment of Head office expenses	110	90	126
Total (A)	2,500	8,889	19,435

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Balance as on 31-03-2015			
- Materials at site	215	152	12
- Plant & Machinery	728	808	3,552
- Work in progress:			
- Value of work certified	2,000	8,600	24,000
- Cost of work not certified	800	452	560
Estimated additional cost	--	--	720
Total (B)	3,743	10,012	28,844
Notional/ estimated profit {(B) – (A)}	1,243	1,123	9,409

(b) Profit to be transferred to Costing Profit and Loss Account for internal purpose:

	Contract-I	Contract-II	Contract-III
Value of Contract	17,500	14,500	24,500
Value of work certified	2,000	8,600	24,000
Percentage of completion (%) $\left(\frac{\text{Work certified}}{\text{Value of contract}} \times 100\right)$	11.43	59.31	97.96
Notional/ Estimated profit	1,243	1,123	9,409
Profit to be transferred to Costing Profit & loss A/c	Nil	636.37 $\left(\frac{2}{3} \times ₹1,123 \times 85\%\right)$	7,484.50 {(9,409 × 97.96% × 85%) - 350}

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

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

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

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

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

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

Workings:

Statement of Equivalent Units (litre):

Input Details	Units	Output details	Units	Equivalent Production					
				Material		Labour		Overheads	
				Units	(%)	Units	(%)	Units	(%)
Opening WIP	800	Units completed:							
Units introduced	5,360	- Opening WIP	800	--	--	240	30	320	40
		- Fresh inputs	3,400	3,400	100	3,400	100	3,400	100
		Normal loss	536	--	--	--	--	--	--
		Abnormal loss	1,264	1,264	100	1,264	100	1,264	100
		Closing WIP	160	160	100	48	30	32	20
	6,160		6,160	4,824		4,952		5,016	

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(d) Process Account for Month

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

7.

Material	SQ* × SP	AQ** × SP	AQ** × AP	RSQ*** × SP
Vita-X	₹ 2,75,000 (2,500 kg. × ₹ 110)	₹ 3,30,000 (3,000 kg. × ₹ 110)	₹ 3,45,000 (3,000 kg. × ₹ 115)	₹ 2,62,460 (2,386 kg. × ₹ 110)
Proto-D	₹ 4,80,000 (1,500 kg. × ₹ 320)	₹ 4,00,000 (1,250 kg. × ₹ 320)	₹ 4,12,500 (1,250 kg. × ₹ 330)	₹ 4,58,240 (1,432 kg. × ₹ 320)
Mine-L	₹ 6,90,000 (1,500 kg. × ₹ 460)	₹ 4,60,000 (1,000 kg. × ₹ 460)	₹ 4,05,000 (1,000 kg. × ₹ 405)	₹ 6,58,720 (1,432 kg. × ₹ 460)
Total	₹ 14,45,000	₹ 11,90,000	₹ 11,62,500	₹ 13,79,420

* *Standard Quantity of materials for actual output :*

Vita-X	$= \frac{5\text{kgs.}}{10\text{kgs}} \times 5{,}000\text{kgs.} = 2{,}500\text{kgs.}$
Proto-D	$= \frac{3\text{kgs.}}{10\text{kgs}} \times 5{,}000\text{kgs.} = 1{,}500\text{kgs.}$
Mine-L	$= \frac{3\text{kgs.}}{10\text{kgs}} \times 5{,}000\text{kgs.} = 1{,}500\text{kgs.}$

** *Actual Quantity of Material used for actual output:*

Vita-X	$= \frac{6\text{kgs.}}{10\text{kgs}} \times 5{,}000\text{kgs.} = 3{,}000\text{kgs.}$
Proto-D	$= \frac{2.5\text{kgs.}}{10\text{kgs}} \times 5{,}000\text{kgs.} = 1{,}250\text{kgs.}$
Mine-L	$= \frac{2\text{kgs.}}{10\text{kgs}} \times 5{,}000\text{kgs.} = 1{,}000\text{kgs.}$

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****Revised Standard Quantity (RSQ):*

Vita-X	$= \frac{5\text{kgs.}}{11\text{ kgs}} \times 5{,}250\text{kgs.} = 2{,}386\text{kgs.}$
Proto-D	$= \frac{3\text{kgs.}}{11\text{kgs}} \times 5{,}250\text{kgs.} = 1{,}432\text{kgs.}$
Mine-L	$= \frac{3\text{kgs.}}{11\text{kgs}} \times 5{,}250\text{kgs.} = 1{,}432\text{kgs.}$

(i) Material Cost Variance = (Std. Qty. × Std. Price) – (Actual Qty. × Actual Price)

Or	= (SQ × SP) – (AQ × AP)		
Vita-X	= ₹ 2,75,000 - ₹ 3,45,000	= ₹ 70,000	(A)
Proto-D	= ₹ 4,80,000 - ₹ 4,12,500	= ₹ 67,500	(F)
Mine-L	= ₹ 6,90,000 - ₹ 4,05,000	= ₹ 2,85,000	(F)
		₹ 2,82,500	(F)

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

	= (AQ × SP) – (AQ × AP)		
Vita-X	= ₹ 3,30,000 - ₹ 3,45,000	= ₹ 15,000	(A)
Proto-D	= ₹ 4,00,000 - ₹ 4,12,500	= ₹ 12,500	(A)
Mine-L	= ₹ 4,60,000 - ₹ 4,05,000	= ₹ 55,000	(F)
		₹ 27,500	(F)

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

Or	= (SQ × SP) – (AQ × SP)		
Vita-X	= ₹ 2,75,000 - ₹ 3,30,000	= ₹ 55,000	(A)
Proto-D	= ₹ 4,80,000 - ₹ 4,00,000	= ₹ 80,000	(F)
Mine-L	= ₹ 6,90,000 - ₹ 4,60,000	= ₹ 2,30,000	(F)
		₹ 2,55,000	(F)

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

Or	= (RSQ × SP) – (AQ × SP)		
Vita-X	= ₹ 2,62,460 - ₹ 3,30,000	= ₹ 67,540	(A)
Proto-D	= ₹ 4,58,240 - ₹ 4,00,000	= ₹ 58,240	(F)
Mine-L	= ₹ 6,58,720 - ₹ 4,60,000	= ₹ 1,98,720	(F)
		= ₹ 1,89,420	(F)

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(v) Material Yield Variance = Std. Price (Std. Qty. – Revised Std. Qty.)

Or = (SQ × SP) – (RSQ × SP)

Vita-X	= ₹ 2,75,000 - ₹ 2,62,460	= ₹ 12,540	(F)
Proto-D	= ₹ 4,80,000 - ₹ 4,58,240	= ₹ 21,760	(F)
Mine-L	= ₹ 6,90,000 - ₹ 6,58,720	= ₹ 31,280	(F)
		= ₹ 65,580	(F)

8. (a) Statement of Profit under Absorption Costing

Particulars	April (₹)	May (₹)	June (₹)
Sales (units)	4,200	4,500	5,200
Selling price per unit	2,050	2,050	2,050
Sales value (A)	86,10,000	92,25,000	1,06,60,000
Cost of Goods Sold:			
- Opening Stock @ ₹1,480	0	5,92,000	4,44,000
- Production cost @ ₹1,480	68,08,000	65,12,000	81,40,000
- Closing Stock @ ₹1,480	(5,92,000)	(4,44,000)	(8,88,000)
- Under/ (Over) absorption	40,000	60,000	(50,000)
Add: Fixed Selling Overheads	95,000	95,000	95,000
Cost of Sales (B)	63,51,000	68,15,000	77,41,000
Profit (A – B)	22,59,000	24,10,000	29,19,000

Workings:

1. Calculation of full production cost

	(₹)
Direct Materials (4 kg. × ₹ 120)	480
Direct labour (6 hours × ₹ 60)	360
Variable production Overhead (150% of ₹ 360)	540
Total Variable cost	1,380
Fixed production overhead $\left(\frac{₹60,00,000}{60,000\text{ units}}\right)$	100
	1,480

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2. Calculation of Opening and Closing stock

	April	May	June
Opening Stock	0	400	300
Add: Production	4,600	4,400	5,500
Less: Sales	4,200	4,500	5,200
Closing Stock	400	300	600

3. Calculation of Under/Over absorption of fixed production overhead

	April (₹)	May (₹)	June (₹)
Actual Overhead	5,00,000	5,00,000	5,00,000
Overhead absorbed	4,60,000 (4,600 units × ₹100)	4,40,000 (4,600 units × ₹100)	5,50,000 (4,600 units × ₹100)
Under/(Over) absorption	40,000	60,000	(50,000)

(b) Statement of Profit under Marginal Costing

Particulars	April (₹)	May (₹)	June (₹)
Sales (units)	4,200	4,500	5,200
Selling price per unit	2,050	2,050	2,050
Sales value	86,10,000	92,25,000	1,06,60,000
Less: Variable production cost	57,96,000	62,10,000	71,76,000
Contribution	28,14,000	30,15,000	34,84,000
Less: Fixed Production Overheads	5,00,000	5,00,000	5,00,000
Less: Fixed Selling Overheads	95,000	95,000	95,000
Profit	22,19,000	24,20,000	28,89,000

(c) Reconciliation of profit under Absorption costing to Marginal Costing

Particulars	April (₹)	May (₹)	June (₹)
Profit under Absorption Costing	22,59,000	24,10,000	29,19,000
Add: Opening Stock	0	40,000 (400 × ₹ 100)	30,000 (300 × ₹ 100)
Less: Closing Stock	40,000 (400 × ₹ 100)	30,000 (300 × ₹ 100)	60,000 (600 × ₹ 100)
Profit under Marginal Costing	22,19,000	24,20,000	28,89,000

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9. (a) (i) Production Budget (in units) for the year ended 31st March 2016

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

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

	Product M	Product N
No. of units to be produced	29,500	14,000
Usage of Material Z per unit of production	5 kg.	6 kg.
Material needed for production	1,47,500 kg.	84,000 kg.
Materials to be purchased	1,63,889 kg. $\left(\frac{1,47,500}{0.90}\right)$	88,421 kg. $\left(\frac{84,000}{0.95}\right)$
Total quantity to be purchased	2,52,310 kg.	
Rate per kg. of Material Z	₹36	
Total purchase price	₹90,83,160	

(b) Calculation of Economic Order Quantity for Material Z

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

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

= 4,000 kg. × 40 orders = 1,60,000 kg.

	Product M	Product N
Material needed for production to maintain the same production mix	1,03,929 kg. $\left(1,60,000 \times \frac{1,63,889}{2,52,310}\right)$	56,071 kg. $\left(1,60,000 \times \frac{88,421}{2,52,310}\right)$

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Less: Process wastage	10,393 kg.	2,804 kg.
Net Material available for production	93,536 kg.	53,267 kg.
Units to be produced	18,707 units $\left(\frac{93,536\,kg.}{5\,kg.}\right)$	8,878 units $\left(\frac{53,267\,kg.}{6\,kg.}\right)$

10. (a) Definition of product costs: Product costs are inventoriable costs. These are the costs, which are assigned to the product. Under marginal costing variable manufacturing costs and under absorption costing, total manufacturing costs constitute product costs.

Purposes for computing product costs:

The three different purposes for computing product costs are as follows:

(i) *Preparation of financial statements:* Here focus is on inventoriable costs.

(ii) *Product pricing:* It is an important purpose for which product costs are used. For this purpose, the cost of the areas along with the value chain should be included to make the product available to the customer.

(iii) *Contracting with government agencies:* For this purpose government agencies may not allow the contractors to recover research and development and marketing costs under cost plus contracts.

(b) Operating Costs are the costs incurred by undertakings which do not manufacture any product but provide a service. Such undertakings for example are — Transport concerns, Gas agencies; Electricity Undertakings; Hospitals; Theatres etc. Because of the varied nature of activities carried out by the service undertakings, the cost system used is obviously different from that followed in manufacturing concerns.

The essential features of operating costs are as follows:

(1) The operating costs can be classified under three categories. For example in the case of transport undertaking these three categories are as follows:

(a) Operating and running charges: It includes expenses of variable nature. For example expenses on petrol, diesel, lubricating oil, and grease etc.

(b) Maintenance charges: These expenses are of semi-variable nature and includes the cost of tyres and tubes, repairs and maintenance, spares and accessories, overhaul, etc.

(c) Fixed or standing charges: These includes garage rent, insurance, road licence, depreciation, interest on capital, salary of operating manager, etc.

(2) The cost unit used is composite like passenger-mile; Kilowatt-hour, etc.

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It can be implemented in all firms of transport, airlines, bus-service, etc., and by all firms of distribution undertakings.

(c) Apportionment of Joint Cost amongst Joint Products using:

Market value at the point of separation

This method is used for apportionment of joint costs to joint products upto the split off point. It is difficult to apply if the market value of the product at the point of separation is not available. It is useful method where further processing costs are incurred disproportionately.

Net realizable value Method

From the sales value of joint products (at finished stage) the followings are deducted:

– Estimated profit margins

– Selling & distribution expenses, if any

– Post split off costs.

The resultant figure so obtained is known as net realizable value of joint products. Joint costs are apportioned in the ratio of net realizable value.

(d) (i) Pre-production Costs: These costs forms the part of development cost, incurred in making a trial production run, preliminary to formal production. These costs are incurred when a new factory is in the process of establishment or a new project is undertaken or a new product line or product is taken up, but there is no established or formal production to which such costs may be charged.

(ii) Research and Development Costs: Research costs are the costs incurred for the original and planned investigation undertaken with a prospect of gaining new scientific or technical knowledge and understanding.

Development costs are the cost incurred in applying research findings or other knowledge to a plan or design for the production of new or substantially improved materials, devices, products, processes, systems or services prior to the commencement of commercial production or use.

(iii) Training Costs: Costs which are incurred in and in relation to providing training to the workers, apprentices, executives etc. Training cost consists of wages and salaries paid to new trainees, fees paid to trainers, cost of materials and properties used to train the trainees, costs associated with training centre, loss suffered due to lower production and extra spoilage etc. The total cost of training section is thereafter apportioned to production centers.

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PART II: FINANCIAL MANAGEMENT

QUESTIONS

Time Value of Money

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

   (i) What amount to be deposited today or

   (ii) What amount must be deposited annually?

Ratio Analysis

2. Based on the following particulars show various assets and liabilities of Tirupati Ltd.

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

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

Cash Flow Analysis

3. Balance Sheets of RIO Ltd. as on 31st March, 2014 and 2015 were as follows:

Liabilities	31.3.14 (₹)	31.3.15 (₹)	Assets	31.3.14 (₹)	31.3.15 (₹)
Equity Share Capital	10,00,000	10,00,000	Goodwill	1,00,000	80,000
8% Preference Share Capital	2,00,000	3,00,000	Land and Building	7,00,000	6,50,000
General Reserve	1,20,000	1,45,000	Plant & Machinery	6,00,000	6,60,000
Securities Premium	--	25,000	Investments (non-trading)	2,40,000	2,20,000
Profit and Loss A/c	2,10,000	3,00,000	Stock	4,00,000	3,85,000
11% Debentures	5,00,000	3,00,000	Debtors	2,88,000	4,15,000
Creditors	1,85,000	2,15,000	Cash and Bank	88,000	93,000

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Provision for tax	80,000	1,05,000	Prepaid Expenses	15,000	11,000
Proposed Dividend	1,36,000	1,44,000	Premium on Redemption of Debentures	--	20,000
	24,31,000	25,34,000		24,31,000	25,34,000

Additional Information:

1. Investments were sold during the year at a profit of ₹ 15,000.
2. During the year an old machine costing ₹ 80,000 was sold for ₹ 36,000. Its written down value was ₹ 45,000.
3. Depreciation charged on Plants and Machinery @ 20 per cent on the opening balance.
4. There was no purchase or sale of Land and Building.
5. Provision for tax made during the year was ₹ 96,000.
6. Preference shares were issued for consideration of cash during the year.

You are required to prepare:

(i) Cash flow statement as per AS- 3.

(ii) Schedule of Changes in Working Capital.

Cost of Capital

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

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

You are required:

(a) To ascertain the pattern for raising the additional finance.

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(b) To calculate the post-tax average cost of additional debt.

(c) To calculate the cost of retained earnings and cost of equity, and

(d) Find out the overall weighted average cost of capital (after tax).

Capital Structure Decisions

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

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

Leverage

6. A firm has sales of ₹ 75,00,000 variable cost is 56% and fixed cost is ₹ 6,00,000. It has a debt of ₹ 45,00,000 at 9% and equity of ₹ 55,00,000.

   (i) What is the firm's ROI?

   (ii) Does it have favourable financial leverage?

   (iii) If the firm belongs to an industry whose capital turnover is 3, does it have a high or low capital turnover?

   (iv) What are the operating, financial and combined leverages of the firm?

   (v) If the sales is increased by 10% by what percentage EBIT will increase?

   (vi) At what level of sales the EBT of the firm will be equal to zero?

   (vii) If EBIT increases by 20%, by what percentage EBT will increase?

Capital Budgeting

7. BT Pathology Lab Ltd. is using a X-ray machines which reached at the end of their useful lives. Following new X-ray machines of two different brands with same features are available for the purchase.

Brand	Cost of Machine	Life of Machine	Maintenance Cost			Rate of Depreciation
			Year 1-5	Year 6-10	Year 11-15	
XYZ	₹6,00,000	15 years	₹ 20,000	₹ 28,000	₹ 39,000	4%
ABC	₹4,50,000	10 years	₹ 31,000	₹ 53,000	--	6%

   Residual Value of both of above machines shall be dropped by 1/3 of Purchase price in the first year and thereafter shall be depreciated at the rate mentioned above.

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Alternatively, the machine of Brand ABC can also be taken on rent to be returned back to the owner after use on the following terms and conditions:

- Annual Rent shall be paid in the beginning of each year and for first year it shall be ₹ 1,02,000.
- Annual Rent for the subsequent 4 years shall be ₹ 1,02,500.
- Annual Rent for the final 5 years shall be ₹ 1,09,950.
- The Rent Agreement can be terminated by BT Labs by making a payment of ₹ 1,00,000 as penalty. This penalty would be reduced by ₹ 10,000 each year of the period of rental agreement.

You are required to:

(a) Advise which brand of X-ray machine should be acquired assuming that the use of machine shall be continued for a period of 20 years.

(b) Which of the option is most economical if machine is likely to be used for a period of 5 years?

The cost of capital of BT Labs is 12%.

Management of Payables (Creditors)

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

Financing of Working Capital

9. Following information is forecasted by the Puja Limited for the year ending 31^{st} March, 2015:

	Balance as at 1^{st} April, 2014 (₹)	Balance as at 31^{st} March, 2015 (₹)
Raw Material	45,000	65,356
Work-in-progress	35,000	51,300
Finished goods	60,181	70,175
Debtors	1,12,123	1,35,000
Creditors	50,079	70,469
Annual purchases of raw material (all credit)		4,00,000

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Annual cost of production		7,50,000
Annual cost of goods sold		9,15,000
Annual operating cost		9,50,000
Annual sales (all credit)		11,00,000

You may take one year as equal to 365 days.

You are required to calculate:

(i) Net operating cycle period.

(ii) Number of operating cycles in the year.

(iii) Amount of working capital requirement using operating cycles.

Miscellaneous

10. (a) "The profit maximization is not an operationally feasible criterion."Comment on it.

(b) Write short notes on the following:

(i) Bridge Finance

(ii) Floating Rate Bonds

(iii) Packing Credit.

(c) "Financial Leverage is a double edged sword" Comment.

SUGGESTED HINTS/ANSWERS

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

$= ₹\ 55,839.48$

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

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

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

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

(b) Cost of Sales = Sales – Gross profit

= ₹ 32,00,000 - ₹ 8,00,000

= ₹ 24,00,000

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

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

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

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

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

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

Average Stock = $\frac{\text{Opening Stock} + \text{Closing Stock}}{2}$

Average Stock = $\frac{\text{Opening Stock} + \text{Opening Stock} + 20,000}{2}$

Average Stock = Opening Stock + ₹ 10,000

Opening Stock = Average Stock - ₹ 10,000

= ₹ 3,00,000 - ₹10,000

= ₹ 2,90,000

Closing Stock = Opening Stock + ₹ 20,000

= ₹ 2,90,000 + ₹ 20,000 = ₹ 3,10,000

(f) Payable turnover = $\frac{\text{Purchase}}{\text{Creditors}} = 6$

Purchases = Cost of Sales + Increase in Stock

= ₹ 24,00,000 + ₹ 20,000 = ₹ 24,20,000

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Creditors = $\frac{\text{Purchase}}{6} = \frac{₹\,24,20,000}{6}$ = ₹ 4,03,333

(g) Capital turnover = $\frac{\text{Cost of Sales}}{\text{Capital Employed}} = 2$

Capital Employed = $\frac{\text{Cost of Sales}}{2} = \frac{₹\,24,00,000}{2}$ = ₹ 12,00,000

(h) Capital = Capital Employed – Reserves & Surplus

= ₹ 12,00,000 – ₹ 2,00,000 = ₹ 10,00,000

Balance Sheet of Tirupati Ltd as on

Liabilities	Amount (₹)	Assets	Amount (₹)
Capital	10,00,000	Fixed Assets	3,00,000
Reserve & Surplus	2,00,000	Stock	3,10,000
Creditors	4,03,333	Debtors	8,00,000
		Other Current Assets	1,93,333
	16,03,333		16,03,333

3. (i) Cash Flow Statement

for the year ending 31st Mach, 2015

	(₹)	(₹)
A. Cash flow from Operating Activities		
Profit and Loss A/c as on 31.3.2015		3,00,000
Less: Profit and Loss A/c as on 31.3.2014		2,10,000
		90,000
Add: Transfer to General Reserve	25,000	
Provision for Tax	96,000	
Proposed Dividend	1,44,000	2,65,000
Profit before Tax		3,55,000
Adjustment for Depreciation:		
Land and Building (on building)	50,000	
Plant and Machinery	1,20,000	1,70,000
Profit on Sale of Investments		(15,000)
Loss on Sale of Plant and Machinery		9,000

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	Goodwill written off		20,000
	Interest on 11% Debentures (see the note)		33,000
	Operating Profit before Working Capital Changes		5,72,000
	Adjustment for Working Capital Changes:		
	Decrease in Prepaid Expenses		4,000
	Decrease in Stock		15,000
	Increase in Debtors		(1,27,000)
	Increase in Creditors		30,000
	Cash generated from Operations		4,94,000
	Income tax paid		(71,000)
	Net Cash Inflow from Operating Activities (a)		4,23,000
B.	Cash flow from Investing Activities		
	Sale of Investment		35,000
	Sale of Plant and Machinery		36,000
	Purchase of Plant and Machinery		(2,25,000)
	Net Cash Outflow from Investing Activities (b)		(1,54,000)
C.	Cash Flow from Financing Activities		
	Issue of Preference Shares		1,00,000
	Securities Premium received on Issue of Pref. Shares		25,000
	Redemption of Debentures at premium		(2,20,000)
	Dividend paid		(1,36,000)
	Interest paid to Debenture holders		(33,000)
	Net Cash Outflow from Financing Activities (c)		(2,64,000)
	Net increase in Cash and Cash Equivalents during the year (a + b + c)		5,000
	Cash and Cash Equivalents at the beginning of the year		88,000
	Cash and Cash Equivalents at the end of the year		93,000

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Working Notes:

1. Provision for the Tax Account

	(₹)		(₹)
To Bank (paid)	71,000	By Balance b/d	80,000
To Balance c/d	1,05,000	By Profit and Loss A/c	96,000
	1,76,000		1,76,000

2. Investment Account

	(₹)		(₹)
To Balance b/d	2,40,000	By Bank A/c (bal. figure)	35,000
To Profit and Loss (Profit on sale)	15,000	By Balance c/d	2,20,000
	2,55,000		2,55,000

3. Plant and Machinery Account

	(₹)		(₹)
To Balance b/d	6,00,000	By Bank (sale)	36,000
To Bank A/c (Purchase bal. figure)	2,25,000	By Profit and Loss A/c (Loss on sale)	9,000
		By Depreciation	1,20,000
		By Balance c/d	6,60,000
	8,25,000		8,25,000

Note: It is assumed that the debentures are redeemed at the beginning of the year.

(ii) Schedule of Changes in Working Capital

Particulars	31st March		Change in Working Capital	
	2014 (₹)	2015 (₹)	Increase (₹)	Decrease (₹)
Current Assets				
Stock	4,00,000	3,85,000	--	15,000
Debtors	2,88,000	4,15,000	1,27,000	--
Prepaid Expenses	15,000	11,000	--	4,000
Cash and Bank	88,000	93,000	5,000	--
Total (A)	7,91,000	9,04,000		

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Current Liabilities				
Creditors	1,85,000	2,15,000	--	30,000
Total (B)	1,85,000	2,15,000		
Working Capital (A – B)	6,06,000	6,89,000		
Increase in Working Capital	83,000	--	--	83,000
	6,89,000	6,89,000	1,32,000	1,32,000

4. (a) Pattern of Raising Additional Finance

Equity = 10,00,000 × 60/100 = ₹ 6,00,000

Debt = 10,00,000 × 40/100 = ₹ 4,00,000

Capital structure after Raising Additional Finance

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

(b) Post-tax Average Cost of Additional Debt

$K_d = I(1 – t)$, where 'K_d' is cost of debt, 'I' is interest and 't' is tax.

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

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

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

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

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

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

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Then, $K_e = \frac{2(1.1)}{44} + 0.10 \quad = \frac{2.2}{44} + 0.10 = 0.15 \text{ or } 15\%$

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

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

5. (i) Valuation under Net Income Approach

Particulars	P Amount (₹)	Q Amount (₹)
Earnings before Interest & Tax (EBIT) (20% of ₹ 30,00,000)	6,00,000	6,00,000
Less: Interest (10% of ₹ 18,00,000)	1,80,000	
Earnings before Tax (EBT)	4,20,000	6,00,000
Less: Tax @ 50%	2,10,000	3,00,000
Earnings after Tax (EAT) (available to equity holders)	2,10,000	3,00,000
Value of equity (capitalized @ 15%)	14,00,000 (2,10,000 × 100/15)	20,00,000 (3,00,000 × 100/15)
Add: Total Value of debt	18,00,000	Nil
Total Value of Company	32,00,000	20,00,000

(ii) Valuation of Companies under Net Operating Income Approach

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

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Value of equity	11,00,000	20,00,000
Add: Total Value of debt	18,00,000	Nil
Total Value of Company	29,00,000	20,00,000

6. Income Statement

Particulars	Amount (₹)
Sales	75,00,000
Less: Variable cost (56% of 75,00,000)	42,00,000
Contribution	33,00,000
Less: Fixed costs	6,00,000
Earnings before interest and tax (EBIT)	27,00,000
Less: Interest on debt (@ 9% on ₹ 45 lakhs)	4,05,000
Earnings before tax (EBT)	22,95,000

(i) ROI $= \dfrac{\text{EBIT}}{\text{Capital employed}} \times 100 \quad = \quad \dfrac{\text{EBIT}}{\text{Equity} + \text{Debt}} \times 100$

$$= \frac{27,00,000}{55,00,000 + 45,00,000} \times 100 = 27\%$$

(ROI is calculated on Capital Employed)

(ii) ROI = 27% and Interest on debt is 9%, hence, it has a favourable financial leverage.

(iii) Capital Turnover $= \dfrac{\text{Net Sales}}{\text{Capital}}$

Or $= \dfrac{\text{Net Sales}}{\text{Capital}} = \dfrac{75,00,000}{1,00,00,000} = 0.75$

Which is very low as compared to industry average of 3.

(iv) Calculation of Operating, Financial and Combined leverages

(a) Operating Leverage $= \dfrac{\text{Contribution}}{\text{EBIT}} = \dfrac{33,00,000}{27,00,000} = 1.22$ (approx)

(b) Financial Leverage $= \dfrac{\text{EBIT}}{\text{EBT}} = \dfrac{27,00,000}{22,95,000} = 1.18$ (approx)

(c) Combined Leverage $= \dfrac{\text{Contribution}}{\text{EBT}} = \dfrac{33,00,000}{22,95,000} = 1.44$ (approx)

Or = Operating Leverage × Financial Leverage = 1.22 × 1.18 = 1.44 (approx)

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(v) Operating leverage is 1.22. So if sales is increased by 10%. EBIT will be increased by 1.22 × 10 i.e. 12.20% (approx)

(vi) Since the combined Leverage is 1.44, sales have to drop by 100/1.44 i.e. 69.44% to bring EBT to Zero

Accordingly, New Sales = ₹ 75,00,000 × (1 - 0.6944)

= ₹ 75,00,000 × 0.3056

= ₹ 22,92,000 (approx)

Hence at ₹ 22,92,000 sales level EBT of the firm will be equal to Zero.

(vii) Financial leverage is 1.18. So, if EBIT increases by 20% then EBT will increase by

1.18 × 20 = 23.6% (approx)

7. Since the life span of each machine is different and time span exceeds the useful lives of each model, we shall use Equivalent Annual Cost method to decide which brand should be chosen.

(i) If machine is used for 20 years

Present Value (PV) of cost if machine of Brand XYZ is purchased

Period	Cash Outflow (₹)	PVF@12%	Present Value
0	6,00,000	1.000	6,00,000
1-5	20,000	3.605	72,100
6-10	28,000	2.045	57,260
11-15	39,000	1.161	45,279
15	(64,000)	0.183	(11,712)
			7,62,927

PVAF for 1-15 years 6.811

Equivalent Annual Cost = $\frac{₹7,62,927}{6.811}$ = ₹ 1,12,014

Present Value (PV) of cost if machine of Brand ABC is purchased

Period	Cash Outflow (₹)	PVF@12%	Present Value
0	4,50,000	1.000	4,50,000
1 - 5	31,000	3.605	1,11,755
6 -10	53,000	2.045	1,08,385
10	(57,000)	0.322	(18,354)
			6,51,786

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PVAF for 1-10 years 5.65

Equivalent Annual Cost = $\frac{₹6,51,786}{5.65}$ = ₹ 1,15,360

Present Value (PV) of cost if machine of Brand ABC is taken on Rent

Period	Cash Outflow (₹)	PVF@12%	Present Value
0	1,02,000	1.000	1,02,000
1 - 4	1,02,500	3.037	3,11,293
5-9	1,09,950	2.291	2,51,895
			6,65,188

PVAF for 1-10 years 5.65

Equivalent Annual Cost = $\frac{₹6,65,188}{5.65}$ = ₹ 1,17,732

Decision: Since Equivalent Annual Cash Outflow is least in case of purchase of Machine of brand XYZ the same should be purchased.

(ii) If machine is used for 5 years

(a) Scrap Value of Machine of Brand XYZ
= ₹ 6,00,000 – ₹ 2,00,000 – ₹ 6,00,000 × 0.04 × 4 = ₹ 3,04,000

(b) Scrap Value of Machine of Brand ABC
= ₹ 4,50,000 – ₹ 1,50,000 – ₹ 4,50,000 × 0.06 × 4 = ₹ 1,92,000

Present Value (PV) of cost if machine of Brand XYZ is purchased

Period	Cash Outflow (₹)	PVF@12%	Present Value
0	6,00,000	1.000	6,00,000
1 - 5	20,000	3.605	72,100
5	(3,04,000)	0.567	(1,72,368)
			4,99,732

Present Value (PV) of cost if machine of Brand ABC is purchased

Period	Cash Outflow (₹)	PVF@12%	Present Value
0	4,50,000	1.000	4,50,000
1-5	31,000	3.605	1,11,755
5	(1,92,000)	0.567	(1,08,864)
			4,52,891

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Present Value (PV) of cost if machine of Brand ABC is taken on Rent

Period	Cash Outflow (₹)	PVF@12%	Present Value
0	1,02,000	1.000	1,02,000
1-4	1,02,500	3.037	3,11,293
5	50,000	0.567	28,350
			4,41,643

Decision: Since Cash Outflow is least in case of lease of Machine of brand ABC the same should be taken on rent.

8. Annual Benefit of accepting the Discount

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

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

If average invoice amount is ₹ 10,00,000

	If discount is	
	Accepted	Not Accepted
Payment to Supplier	98,500	1,00,000
Return on investment of ₹ 98,500 for 30 days {₹ 98,500 × (30/365) × 15%}		(1,214)
	98,500	98,786

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

9. Working Notes:

1. Raw Material Storage Period (R)

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

$$= \frac{\frac{₹\,45{,}000 + ₹\,65{,}356}{2}}{₹\,3{,}79{,}644} \times 365$$

= 53 days.

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

= ₹ 45,000 + ₹ 4,00,000 – ₹ 65,356

= ₹ 3,79,644

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

WIP Conversion Period $= \dfrac{\text{Average Stock of WIP}}{\text{Annual Cost of Production}} \times 365$

$$= \dfrac{\dfrac{₹\,35{,}000 + ₹\,51{,}300}{2}}{₹\,7{,}50{,}000} \times 365$$

= 21 days

3. Finished Stock Storage Period (F)

$$= \dfrac{\text{Average Stock of Finished Goods}}{\text{Cost of Goods Sold}} \times 365$$

$$= \dfrac{₹\ 65{,}178}{₹\,9{,}15{,}000} \times 365 \qquad = 26 \text{ days.}$$

Average Stock $= \dfrac{₹\,60{,}181 + ₹\,70{,}175}{2}$

$= ₹\ 65{,}178.$

4. Debtors Collection Period (D)

$$= \dfrac{\text{Average Debtors}}{\text{Annual Credit Sales}} \times 365$$

$$= \dfrac{₹\ 1{,}23{,}561.50}{₹\ 11{,}00{,}000} \times 365$$

= 41 days

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

5. Creditors Payment Period (C)

$$= \dfrac{\text{Average Creditors}}{\text{Annual Net Credit Purchases}} \times 365$$

$$= \dfrac{\left(\dfrac{₹50{,}079 + ₹70{,}469}{2}\right)}{₹4{,}00{,}000} \times 365 = 55 \text{ days}$$

(i) Operating Cycle Period

= R + W + F+ D – C = 53 + 21 + 26 + 41 – 55 = 86 days

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(ii) Number of Operating Cycles in the Year

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

(iii) Amount of Working Capital Required

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

10. (a) "The profit maximisation is not an operationally feasible criterion."This statement is true because Profit maximisation can be a short-term objective for any organisation and cannot be its sole objective. Profit maximization fails to serve as an operational criterion for maximizing the owner's economic welfare. It fails to provide an operationally feasible measure for ranking alternative courses of action in terms of their economic efficiency. It suffers from the following limitations:

(i) Vague term: The definition of the term profit is ambiguous. Does it mean short term or long term profit? Does it refer to profit before or after tax? Total profit or profit per share?

(ii) Timing of Return: The profit maximization objective does not make distinction between returns received in different time periods. It gives no consideration to the time value of money, and values benefits received today and benefits received after a period as the same.

(iii) It ignores the risk factor.

(iv) The term maximization is also vague

(b) (i) Bridge Finance: Bridge finance refers, normally, to loans taken by the business, usually from commercial banks for a short period, pending disbursement of term loans by financial institutions. Normally it takes time for the financial institution to finalise procedures of creation of security, tie-up participation with other institutions etc. even though a positive appraisal of the project has been made. However, once the loans are approved in principle, firms in order not to lose further time in starting their projects arrange for bridge finance. Such temporary loan is normally repaid out of the proceeds of the principal term loans. It is secured by hypothecation of moveable assets, personal guarantees and demand promissory notes. Generally rate of interest on bridge finance is higher as compared with that on term loans.

(ii) Floating Rate Bonds: These are the bonds where the interest rate is not fixed and is allowed to float depending upon the market conditions. These are ideal instruments which can be resorted to by the issuers to hedge themselves against the volatility in the interest rates. They have become more popular as a money market instrument and have been successfully issued by financial institutions like IDBI, ICICI etc.

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(iii) **Packing Credit**: Packing credit is an advance made available by banks to an exporter. Any exporter, having at hand a firm export order placed with him by his foreign buyer on an irrevocable letter of credit opened in his favour, can approach a bank for availing of packing credit. An advance so taken by an exporter is required to be liquidated within 180 days from the date of its commencement by negotiation of export bills or receipt of export proceeds in an approved manner. Thus Packing Credit is essentially a short-term advance.

(c) On one hand when cost of 'fixed cost fund' is less than the return on investment financial leverage will help to increase return on equity and EPS. The firm will also benefit from the saving of tax on interest on debts etc. However, when cost of debt will be more than the return it will affect return of equity and EPS unfavourably and as a result firm can be under financial distress. This is why financial leverage is known as "double edged sword".

Effect on EPS and ROE:

When	Effect	Result
ROI > Interest	Favourable	Advantage
ROI < Interest	Unfavourable	Disadvantage
ROI = Interest	Neutral	Neither advantage nor disadvantage

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PAPER – 4: TAXATION

PART – I: STATUTORY UPDATE

Significant Notifications and Circulars in income-tax and indirect taxes issued between 1st May 2014 and 30th April, 2015

A. INCOME TAX

I. NOTIFICATIONS

1. Notification of Cost Inflation Index for F.Y.2014-15 [Notification No. 31/2014, dated 11-6-2014]

The Central Government has, in exercise of the powers conferred by clause (v) of *Explanation* to section 48, vide this notification specified the Cost Inflation Index for the financial year 2014-15 as 1024.

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	34.	2014-15	1024

2. Increase in ceiling limit for investment in Public Provident Fund [Notification No. G.S.R. 588 (E), dated 13-8-2014]

In exercise of the powers conferred by Section 3(4) of the Public Provident Fund Act, 1968, the Central Government has increased annual ceiling limit for deposit in PPF A/c from ₹ 1 lakh to ₹ 1.50 lakhs by amending the Public Provident Fund Scheme, 1968.

3. **Rate of depreciation in respect of windmills installed on or after 01.04.2014 [Notification No. 43/2014, dated 16-9-2014]**

   The CBDT has, vide this notification, amended the rate of depreciation on certain renewable energy devices. Accordingly, the following renewable energy devices would be eligible for depreciation @80% from A.Y. 2015-16, if they are installed on or after 1st April 2014 –

   (a) Wind mills and any specially designed devices which run on wind mills

   (b) Any special devices including electric generators and pumps running on wind energy

   This implies that if the aforesaid renewable energy devices were installed on or before 31st March 2014, they would be eligible for depreciation @ 15% from A.Y. 2015-16.

   The applicable rate of depreciation for A.Y. 2014-15 and A.Y. 2015-16, based on date of installation of such renewable energy devices, have been tabulated hereunder for a better understanding of the amendment made vide this notification.

Date of installation	Rate of depreciation	
	A.Y. 2014-15	A.Y. 2015-16
On or before 31.03.2012	80%	15%
Between 1.04.2012 to 31.03.2014	15%	15%
On or after 01.04.2014	N.A	80%

4. **Increase in limit for investment in bank term deposit [Notification No. 63/2014, dated 13-11-2014]**

   Under section 80C(2)(xxi), a deduction is allowed in computing the total income of an assessee, being an individual or a Hindu undivided family, with respect to sums paid or deposited in the previous year as a term deposit:

   - for a fixed period of not less than 5 years with a scheduled bank; and
   - which is in accordance with the scheme framed and notified by the Central Government.

   Accordingly, the Central Government had notified Bank Term Deposit Scheme, 2006. As per Para 3 of the said scheme, the maximum amount an assessee can invest in the term deposit of a scheduled bank is ₹ 1,00,000, in a year.

   The Finance (No.2) Act, 2014 had increased the maximum limit of deduction under section 80C from ₹ 1 lakh to ₹ 1.5 lakh w.e.f. A.Y. 2015-16.

   Accordingly, the Central Government has, vide this notification, increased the maximum limit of investment in term deposit of a specified bank from ₹ 1,00,000 to ₹ 1,50,000 in a year, which would qualify for deduction under section 80C.

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5. **Commissioner of Income-tax (Exemptions) to act as "prescribed authority" for the purposes of section 10(23C)(iv)/(v)/(vi)/(via) [Notification Nos. 75/2014 & 76/2014 dated 1-12-2014]**

   For the purposes of claiming exemption under section 10(23C)(iv) and (v), a fund or institution established for charitable purposes and/or a trust or institution wholly for public religious purposes or wholly for public religious and charitable purposes, requires approval of the "prescribed authority".

   Likewise, for the purposes of claiming exemption under section 10(23C)(vi) and (via), any university or other educational institution, existing solely for educational purposes and not for purposes of profit and any hospital or other institution, existing solely for philanthropic purposes and not for profit motive, requires approval of the "prescribed authority".

   Accordingly, the CBDT has, through these notifications, authorized the Commissioner of Income-tax (Exemptions) to act as "prescribed authority" for the purpose of section 10(23C)(iv)/(v)/(vi)/(via) w.e.f. 15th November, 2014.

6. **Percentage of Government grant for determining whether a university or other educational institution, hospital or other institution referred under section 10(23C)(iiiab)/(iiiac) is substantially financed by the Government prescribed [Notification No. 79/2014, dated 12-12-2014]**

   Income of certain educational institutions, universities and hospitals which exist solely for educational purposes or solely for philanthropic purposes, and not for purposes of profit and **which are wholly or substantially financed by the Government** are exempt under section 10(23C).

   The Finance (No. 2), Act, 2014 inserted an *Explanation* after section 10(23C)(iiiac) to clarify that if the government grant to a university or other educational institution, hospital or other institution during the relevant previous year **exceeds a prescribed percentage of the total receipts** (including any voluntary contributions), of such university or other educational institution, hospital or other institution, as the case may be, then, such university or other educational institution, hospital or other institution shall be considered as being **substantially financed by the Government** for that previous year.

   Accordingly, in exercise of the powers conferred by section 295 read with section 10(23C)(iiiab)/(iiiac), the CBDT has notified Rule 2BBB to provide that any university or other educational institution referred under section 10(23C)(iiiab) and hospital or other institution referred under section 10(23C)(iiiac) shall be considered as being substantially financed by the Government for any previous year, if the Government grant to such university or other educational institution, hospital or other institution **exceeds 50% of the total receipts including any voluntary contributions**, of such university or other educational institution, hospital or other institution, as the case may be, during the relevant previous year.

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7. **Deposit in 'Sukanya Samriddhi Account' eligible for deduction under section 80C(2)(viii) [Notification No. 9/2015, dated 21-1-2015]**

Section 80C provides for deduction from gross total income in respect of sums paid and investments made through specified modes like life insurance premia, Public Provident Fund etc. Under clause (viii) of section 80C(2), deduction is available in respect of sums paid or deposited in the previous year by the assessee as subscription to any such deposit scheme as may be notified by the Central Government.

Accordingly, the Central Government, in exercise of the powers conferred by section 80C(2)(viii) of the Income-tax Act, 1961, has specified the ***'Sukanya Samriddhi Account'*** scheme for the welfare of Girl child.

II. CIRCULARS

1. **Interest under section 234A not chargeable on self assessment tax paid before the due date of filing of return of income [Circular No.2/2015, dated 10-2-2015]**

Interest under section 234A is charged in case of default in furnishing return of income by an assessee. The interest is charged at the specified rate on the amount of tax payable on the total income, as reduced by the amount of advance tax, TDS/TCS, any relief of tax allowed under section 90 and 90A, any deduction allowed under section 91 and any tax credit allowed in accordance with section 115JAA and section 115JD. Since self-assessment tax is not mentioned as a component of tax to be reduced from the amount on which interest under section 234A is chargeable, interest is being charged on the amount of self-assessment tax paid by the assessee even if such tax is paid before the due date of filing of return.

However, it has been held by Hon'ble Supreme Court in the case of *CIT vs Prannoy Roy (2009), 309 ITR 231* that interest under section 234A on default of furnishing return of income shall be payable only on the amount of tax that has not been deposited before the due date of filing of the income-tax return for the relevant assessment year.

Accordingly, the CBDT reviewed the present practice of charging interest and decided that no interest under section 234A shall be charged on self assessment tax paid by the assessee before the due date of filing of return.

2. **Clarification regarding disallowance of 'other sum chargeable' under section 40(a)(i) [Circular No.3/2015, dated 12-02-2015]**

If there has been a failure in deduction or in payment of tax deducted in respect of any interest, royalty, fees for technical services or other sum chargeable under the Act either payable in India to a non-corporate non-resident or a foreign company or payable outside India, then, disallowance of the related expenditure/payment is attracted under section 40(a)(i) while computing income chargeable under the head "Profits and gains of business or profession".

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The interpretation of the term 'other sum chargeable' in section 195 has been clarified in this circular i.e. whether this term refers to the whole sum being remitted or only the portion representing the sum chargeable to income-tax under the Act.

In its Instruction No.2/2014, dated 26.02.2014, the CBDT has clarified that the Assessing Officer shall determine the appropriate portion of the sum chargeable to tax as mentioned in section 195(1), to ascertain the tax liability on which the deductor shall be deemed to be an assessee-in-default under section 201, in cases where no application is filed by the deductor for determining the sum so chargeable under section 195(2).

In this circular, the CBDT has, in exercise of its powers under section 119, clarified that for the purpose of making disallowance of 'other sum chargeable' under section 40(a)(i), the appropriate portion of the sum which is chargeable to tax shall form the basis of disallowance. Further, the appropriate portion shall be the same as determined by the Assessing Officer having jurisdiction for the purpose of section 195(1). Also, where the determination of 'other sum chargeable' has been made under sub-section (2), sub-section (3) or sub-section (7) of section 195, such a determination will form the basis for disallowance, if any, under section 40(a)(i).

3. **Clarification regarding applicability of *Explanation 5* to section 9(1)(i) to dividend declared and paid by a foreign company outside India in respect of shares which derive its value substantially from the assets located in India [Circular No. 4/2015, dated 26-03-2015]**

Section 9 provides for incomes which are deemed to accrue or arise in India. As per section 9(1)(i), all income accruing or arising, whether directly or indirectly, through or from any business connection in India, or through or from any property in India, or through or from any asset or source of income in India, or through the transfer of a capital asset situated in India is deemed to accrue or arise in India.

Explanation 5 to section 9(1)(i) was inserted by the Finance Act, 2012 to clarify that an asset or a capital asset being any share or interest in a company or entity registered or incorporated outside India shall be deemed to be and shall always be deemed to have been situated in India, if the share or interest derives, directly or indirectly, its value substantially from the assets located in India".

The Explanatory Memorandum to the Finance Bill, 2012 clearly provides that the amendment of section 9(1)(i) was to reiterate the legislative intent in respect of taxability of gains having economic nexus with India irrespective of the mode of realisation of such gains. Thus, the amendment sought to clarify the source rule of taxation in respect of income arising from indirect transfer of assets situated in India.

Accordingly, Explanation 5 would be applicable in relation to deeming any income arising outside India from any transaction in respect of any share or interest in a foreign company or entity, which has the effect of transferring, directly or indirectly, the underlying assets located in India, as income accruing or arising in India.

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Declaration of dividend by a foreign company outside India, however, does not have the effect of transfer of any underlying assets located in India. This circular, therefore, clarifies that **the dividends declared and paid by a foreign company outside India in respect of shares which derive their value substantially from assets situated in India would NOT be deemed to be income accruing or arising in India by virtue of the provisions of Explanation 5 to section 9(1)(i).**

4. **Applicability of tax on capital gains in the hands of the unit holders where the term of the units of Mutual Funds under the Fixed Maturity Plans has been extended [Circular No. 6/2015, dated 09-04-2015]**

   Fixed Maturity Plans (FMPs) are closed ended funds having a fixed maturity date wherein the duration of investment is decided upfront. Prior to amendment by the Finance (No. 2) Act, 2014, units of a mutual fund under the FMPs held for a period of more than twelve months qualified as long term capital asset. The amendment in sub-section (42A) of section 2 by the Finance (No. 2) Act, 2014 required the period of holding in case of unlisted shares and units of a mutual fund [other than an equity oriented fund] to be more than thirty-six months to qualify as long term capital asset.

   As a result, gains arising out of any investment in the units of FMPs made earlier and sold/redeemed after 10.07.2014 would be taxed as short term capital gains if the unit was held for a period of thirty-six months or less. To enable the FMPs to qualify as a long term capital asset, some Asset Management Companies (AMCs) administering mutual funds have offered extension of the duration of the FMPs to a date beyond thirty-six months from the date of the original investment by providing to the investor an option of roll-over of FMPs in accordance with the provisions of Regulation 33(4) of the SEBI (Mutual Funds) Regulation, 1996.

   The CBDT has, vide this Circular, clarified that the roll over in accordance with the aforesaid regulation will not amount to transfer as the scheme remains the same. Accordingly, no capital gains will arise at the time of exercise of the option by the investor to continue in the same scheme. The capital gains will, however, arise at the time of redemption of the units or opting out of the scheme, as the case may be.

5. **Non-applicability of TDS provisions on payments made to Corporations whose income is exempt under section 10(26BBB) [Circular No. 7/2015, dated 23-04-2015]**

   The CBDT had earlier issued Circular No. 4/2002 dated 16.07.2002 which laid down that there would be no requirement for tax deduction at source in respect of payments made to such entities, whose income is unconditionally exempt under section 10 of the Income-tax Act, 1961 and who are statutorily not required to file return of income as per the section 139. The said Circular also lists the entities which are unconditionally exempt under section 10 and who are statutorily not required to file return of income as per section 139.

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Subsequently, section 10(26BBB) was inserted in the Income-tax Act, 1961 vide Finance Act, 2003 w.e.f. 01.04.2004 to provide that any income of a corporation established by a Central, State or Provincial Act for the welfare and economic upliftment of ex-servicemen being the citizens of India does not form part of the total income.

The corporations covered under section 10(26BBB) satisfy the two conditions of Circular No. 4/2002 i.e., such corporations are statutorily not required to file return of income as per section 139 and their income is also unconditionally exempt under section 10. Accordingly, the CBDT has extended the benefit of the said Circular to such corporations whose income is exempt under section 10(26BBB). Hence, there would be no requirement for tax deduction at source from the payments made to such corporations, since their income is in any case exempt under the Income-tax Act, 1961.

B. INDIRECT TAXES

Basic concepts of indirect taxes – Central Excise Duty

1. **Central excise registration to be granted online within 2 working days** [1*]

   With effect from 01.03.2015, only an online application can be made for obtaining central excise registration and the same will be granted within two working days of the receipt of a duly completed application form. Verification of documents and premises, as the case may be, can be carried out after the grant of the registration *[Notification No. 7/2015 CE (NT) dated 01.03.2015].*

   [Effective from 01.03.2015]

2. **Authentication of invoices by digital signatures** [*]

   An invoice issued under central excise law by a manufacturer may now be authenticated by means of a digital signature. However, where the duplicate copy of the invoice meant for transporter is digitally signed, a hard copy of the duplicate copy of the invoice meant for transporter and self attested by the manufacturer would be used for transport of goods *[Notification No. 8/2015 CE (NT) dated 01.03.2015]*.

   [Effective from 01.03.2015]

Basic concepts of service tax

1. **Clarification regarding levy of service tax on joint venture**

   CBEC has issued following clarification regarding levy of service tax on joint venture:

   (i) **Services provided by the members of the Joint Venture (JV) to the JV and *vice versa* or between the members of the JV:** In accordance with Explanation 3(a) of

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[*] *It may be noted that the procedures under central excise have been discussed in detail at the Final level. At the level of Intermediate (IPC), only a bird's eye view of the significant procedures under central excise has been given to familiarize the students with the basic aspects of such procedures.*

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the definition of service under section 65B(44) of the Finance Act, 1994, JV (an unincorporated temporary association constituted for the limited purpose of carrying out a specified project) and the members of the JV are treated as distinct persons and therefore, taxable services provided for consideration, by the JV to its members or *vice versa* and between the members of the JV are taxable.

(ii) Cash calls (capital contributions) made by the members to the JV: If cash calls are merely a transaction in money, they are excluded from the definition of service provided in section 65B(44) of the Finance Act, 1994. Whether a 'cash call' is 'merely a transaction in money' [in terms of section 65B(44) of the Finance Act, 1994] and hence not in the nature of consideration for taxable service, would depend on the comprehensive examination of the Joint Venture Agreement, which may vary from case to case. Detailed and close scrutiny of the terms of JV agreement may be required in each case, to determine the service tax treatment of cash calls.

[Circular No. 179/5/2014 ST dated 24.09.2014]

Exemptions and Abatements

2. Mega Exemption Notification amended

Mega Exemption *Notification No. 25/2012 ST dated 20.06.2012* has been amended vide ***Notification No. 6/2015 ST dated 01.03.2015, unless specified otherwise.*** The amendments are discussed in the following two broad categories:

(A) New exemptions

(B) Exemptions withdrawn/restricted

(A) <u>NEW EXEMPTIONS</u>

(i) Ambulance services provided by all service providers (whether or not by clinical establishment or an authorised medical practitioner or paramedics) exempted

Earlier, entry 2 exempted any service provided by way of transportation of a patient to and from a clinical establishment from service tax only when the said service was provided by a clinical establishment or an authorised medical practitioner or paramedics.

The scope of this exemption has now been widened to extend the said exemption to ambulance services provided by all service providers. Therefore, now the ambulance services provided by an entity which is not a clinical establishment or an authorised medical practitioner or paramedics would also be exempt from service tax. The above amendment has been made by substituting entry 2 with a new entry.

[Effective from 01.04.2015]

(ii) General insurance provided under Pradhan Mantri Suraksha Bima Yojna exempted

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Entry 26 exempts services of general insurance business provided under specified schemes. A new clause (p) has been inserted vide *Notification No. 12/2015 ST dated 30.04.2015* in the said entry to exempt services of general insurance business provided under Pradhan Mantri Suraksha Bima Yojna.

[Effective from 30.04.2015]

(iii) Life insurance provided under *Varishtha Pension Bima Yojna, Pradhan Mantri Jeevan Jyoti Bima Yojna* and *Pradhan Mantri Jan Dhan Yojna* exempted

Entry 26A exempts services of life insurance business provided under specified schemes. Clauses (d), (e) and (f) have been inserted in the said entry to exempt services of life insurance business provided in respect of the following additional schemes:

Clause (d) Varishtha Pension Bima Yojna - *[Effective from 01.04.2015]*

Clause (e) Pradhan Mantri Jeevan Jyoti Bima Yojna – *[Effective from 30.04.2015* vide *Notification No. 12/2015 ST dated 30.04.2015]*

Clause (f) Pradhan Mantri Jan Dhan Yojna - *[Effective from 30.04.2015* vide *Notification No. 12/2015 ST dated 30.04.2015]*

(iv) Collection of contribution under Atal Pension Yojna (APY) exempted

A new entry 26B has been inserted in the notification vide *Notification No. 12/2015 ST dated 30.04.2015* to exempt the services by way of collection of contribution under Atal Pension Yojna.

[Effective from 30.04.2015]

(v) Treatment of effluent by Common Effluent Treatment Plant operator exempted

A new entry 43 has been inserted in the notification to exempt the services by operator of Common Effluent Treatment Plant by way of treatment of effluent.

[Effective from 01.04.2015]

(vi) Pre-conditioning, pre-cooling, ripening, waxing, retail packing, labelling of fruits and vegetables exempted

A new entry 44 has been inserted in the notification to exempt the services by way of pre-conditioning, pre-cooling, ripening, waxing, retail packing, labelling of fruits and vegetables which do not change or alter the essential characteristics of the said fruits or vegetables.

[Effective from 01.04.2015]

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(vii) Admission to a museum, national park, wildlife sanctuary, tiger reserve or zoo exempted

Services provided by way of admission to a museum, zoo, national park, wild life sanctuary and a tiger reserve have been exempted. A new entry 45 has been inserted in the notification to give effect to this exemption.

Following definitions have been also been inserted in the notification pursuant to the said exemption:

1. *National park has the meaning assigned to it in the clause (21) of the section 2 of The Wild Life (Protection) Act, 1972 [Clause (xaa)].*
2. *Wildlife sanctuary means sanctuary as defined in the clause (26) of the section 2 of The Wild Life (Protection) Act, 1972 [Clause (zk)].*
3. *Zoo has the meaning assigned to it in the clause (39) of the section 2 of the Wild Life (Protection) Act, 1972 [Clause (zl)].*

   Section 2(39) of the Wild Life (Protection) Act, 1972 provides that "Zoo" means an establishment, whether stationary or mobile, where captive animals are kept for exhibition to the public but does not include a circus and an establishment of a licenced dealer in captive animals.
4. *Tiger reserve has the meaning assigned to it in clause (e) of section 38K of the Wild Life (Protection) Act, 1972 [Clause (zi)].*

[Effective from 01.04.2015]

(viii) Exhibition of movie by exhibitor to distributor/ association of persons consisting of such exhibitor as one of its members exempted

Service provided by way of exhibition of movie by an exhibitor to the distributor or an association of persons consisting of the exhibitor as one of its members has been exempted. A new entry 46 has been inserted in the notification to give effect to this exemption.

[Effective from 01.04.2015]

(ix) Service provided with respect to Kailash Mansarovar and Haj pilgrimage exempted

Services provided by a specified organisation in respect of a religious pilgrimage facilitated by the Ministry of External Affairs of the Government of India, under bilateral arrangement, have been exempted from service tax vide *Notification No. 17/2014 ST dated 20.08.2014.*

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Specified organisation means:

(a) Kumaon Mandal Vikas Nigam Limited, a Government of Uttarakhand Undertaking; or

(b) Haj Committee of India and State Haj Committees constituted under the Haj Committee Act, 2002, for making arrangements for the pilgrimage of Muslims of India for Haj.

Thus, the religious pilgrimage organized by the Haj Committee and Kumaon Mandal Vikas Nigam Ltd. are not liable to service tax.

[Effective from 20.08.2014]

(B) EXEMPTIONS WITHDRAWN/RESTRICTED

(i) **Service tax payable on a performance in folk or classical art forms of music/ dance/ theatre if the consideration therefor exceeds ₹ 1,00,000**

Earlier, services by a performing artist in folk or classical art forms of (i) music, or (ii) dance, or (iii) theatre, excluding services provided by such artist as a brand ambassador was exempt from service tax under entry 16 of the notification.

The scope of the said exemption has now been restricted by fixing a monetary limit of ₹ 1,00,000 in respect of a performance.Thus, now exemption to services provided by a performing artist in folk or classical art forms of (i) music, or (ii) dance, or (iii) theatre, will be limited only to such cases where amount charged is upto ₹ 1,00,000 for a performance. However, services provided by an artist as brand ambassador will continue to remain taxable.

[Effective from 01.04.2015]

(ii) **Exemption to transportation of food stuff by rail or vessels or road limited to milk, salt and food grain including flours, pulses and rice**

Earlier, transportation of foodstuff - including flours, tea, coffee, jaggery, sugar, milk products, salt and edible oil, excluding alcoholic beverages - by rail/ vessel and by goods carriage was exempt from service tax under entry 20(i) and entry 21(d) of the notification respectively.

Entry 20(i) and entry 21(d) have been amended to restrict such exemption to transportation of only milk, salt and food grain including flours, pulses and rice by rail/ vessel and by goods carriage. Transportation of agricultural produce by rail or a vessel and by goods carriage is separately exempt vide entry 20(h) and entry 21(a) respectively, and this exemption would continue.

[Effective from 01.04.2015]

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(iii) **Exemption to services by (i) mutual fund agent/distributor to a mutual fund or asset management company and (ii) selling/ marketing agent of lottery tickets to a distributor/selling agent, withdrawn**

Earlier, services by the following persons in their respective capacities were exempt from service tax under entry 29 of the notification:-

(i) mutual fund agent to a mutual fund or asset management company

(ii) distributor to a mutual fund or asset management company

(iii) selling or marketing agent of lottery tickets to a distributor or a selling agent.

The said exemption has now been withdrawn by omitting clause (c), (d) and (e) of entry 29 from the notification. Thus, service tax will be payable on these services.

[Effective from 01.04.2015]

(v) **Exemption withdrawn for services by way of making telephone calls from departmentally run public telephone etc.**

Exemption has been withdrawn in respect of services by way of making telephone calls from-

(a) departmentally run public telephone;

(b) guaranteed public telephone operating only for local calls; or

(c) free telephone at airport and hospital where no bills has been issued.

Entry 32 of the notification has been omitted to give effect to this amendment.

[Effective from 01.04.2015]

3. **Abatement Notification amended**

Abatement *Notification No. 26/2012 ST dated 20.06.2012* has been amended vide *Notification No. 8/2015 ST dated 01.03.2015* as under:

(i) **Uniform abatement of 70% prescribed for (i) goods and passenger transport by rail and (ii) goods transport by road and vessel, subject to uniform condition of non-availment of CENVAT credit on inputs, capital goods and input services**

Earlier, service tax was payable on 30% of the value of rail transport for goods and passengers, 25% of the value of goods transport by road by a goods transport agency (GTA) and 40% for goods transport by vessels. The conditions prescribed also varied.

A uniform abatement of 70% has now been prescribed for (i) transport of goods and passengers by rail and (ii) transport of goods by road by a GTA and vessel alongwith a uniform condition of non-availment of CENVAT credit on inputs, capital goods and input services, used for providing the taxable service. In case of goods

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transport by road by a GTA, the condition for non-availment of CENVAT is for service provider.

Thus, in effect, the abatement percentage has increased from 60 to 70 in case of goods transport by vessel and reduced from 75 to 70 in case of goods transport by road by a goods transport agency. The percentage of abatement however, has remained unaffected in case of rail transport of goods and passengers (70%). Further, while the condition of non-availment of CENVAT credit was present in the case of road and vessel transport of goods earlier also, the same has been introduced newly in case of rail transport of goods and passengers.

[Effective from 01.04.2015]

(ii) Abatement in case of passenger transportation by air in non-economy class reduced from 60% to 40%

Earlier, service tax was payable on 40% of the value of air transport of passengers for economy as well as higher classes, like business class.

Such abatement has now been bifurcated into two categories:-

(a) Abatement for transport of passengers by air, with or without accompanied belongings in economy class - 60%

(b) Abatement for transport of passengers by air, with or without accompanied belongings in other than economy class - 40%

Thus, in effect, abatement for classes other than economy has been reduced by 20% and therefore, service tax would be payable on 60% of the value of air travel in such higher classes.

[Effective from 01.04.2015]

(iii) No abatement for services provided in relation to chit

Earlier, in respect of services provided in relation to chit, service tax was payable on 30% of the value of taxable service under entry 8 of the notification.

However, the abatement of 70% has now been withdrawn from services provided in relation to chit by omitting entry 8. Consequently, service tax would be paid by the chit fund foremen on the full consideration received by way of fee, commission or any such amount. They would be entitled to take CENVAT credit.

[Effective from 01.04.2015]

4. GTA service provided for transport of export goods by road from place of removal/ CFS/ICD to land customs station exempted

Earlier, *Notification No. 31/2012 ST dated 20.06.2012* exempted the goods transport agency service provided for transport of export goods by road from

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- the place of removal to an inland container depot (ICD), a container freight station (CFS), a port or airport;
- any CFS or ICD to the port or airport.

Scope of this exemption has been widened vide *Notification No. 4/2015 ST dated 01.03.2015* to exempt such services when provided for transport of export goods by road from the place of removal or from any CFS/ICD to a land customs station (LCS) also.

[Effective from 01.04.2015]

5. Notification exempting service provided by a foreign commission agent to an Indian exporter rescinded *[Notification No. 42/2012 ST dated 29.6.2012 rescinded]*

Services provided by a commission agent located outside India to an exporter of goods located in India were exempted vide *Notification No. 42/2012 ST dated 29.6.2012.* However, with effect from 01.10.2014, such services became non-taxable as the place of provision of such service shifted to non-taxable territory. Consequently, there remained no need of any exemption for the said service.

Therefore, since this exemption became redundant[2], *Notification No. 42/*2012 *ST dated 29.6.2012* has been rescinded vide *Notification No. 3/2015 ST dated 01.03.2015*.

[Effective from 01.03.2015]

Service tax procedures

6. Following amendments have been made in Service Tax Rules, 1994 vide *Notification No. 5/2015 ST dated 01.03.2015, unless specified otherwise:*

(i) Concept of aggregator introduced in service tax

The word 'aggregate' literally means a whole formed by combining several elements, formed by the combination of many separate items or units. The aggregator is one, who therefore aggregates or causes aggregation of units, items, things or services.

There are also many online websites that follow 'aggregator' model. Under this model, an entity collects or aggregates information on a particular service from several sources on a single platform and draws customers to its platform to connect them with the service provider. It may also facilitate the customers in comparing the

[2] *The exemption to the service provided by a foreign commission agent to an Indian exporter of goods became redundant on account of the amendment made in the Place of Provision of Services Rules, 2012. By virtue of the said amendment, the place of provision of such services shifted from taxable territory (location of service receiver – Indian exporter) to non-taxable territory (location of service provider – foreign commission agent). It may be noted that the Place of Provision of Services Rules, 2012 is outside the scope of syllabus of Part II: Indirect Taxes of Paper 4: Taxation.*

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prices and specifications of a particular service offered by multiple service providers.

Therefore, companies which act as aggregator for service providers like travel portals, food portals or cab services will now be liable to pay service tax.

(a) Definition of aggregator and brand name inserted in rule 2 [Rule 2(1)]

Amendments have been made in Service Tax Rules to bring such aggregator within the service tax net. The definition of "aggregator" has been provided by inserting clause (aa) in rule 2(1) as under-

"Aggregator means a person, who owns and manages a web based software application, and by means of the application and a communication device, enables a potential customer to connect with persons providing service of a particular kind under the brand name or trade name of the aggregator" [Rule 2(1)(aa)]

Accordingly, "brand name or trade name" has also been defined by inserting clause (bca) in rule 2(1) as under:

"Brand name or trade means a brand name or a trade name whether registered or not, that is to say, a name or a mark, such as an –

- *invented word or writing,*
- *or a symbol,*
- *monogram,*
- *logo,*
- *label,*
- *signature,*

which is used for the purpose of indicating, or so as to indicate a connection, in the course of trade, between a service and some person using the name or mark with or without any indication of the identity of that person" [Rule 2(1)(bca)].

[Effective from 01.03.2015]

(b) Aggregator to pay service tax under reverse charge [Rule 2(1)(d)(i)(AAA)]

Rule 2(1)(d)(i) defines the term "person liable for paying service tax" in respect of the taxable services notified under section 68(2) of Finance Act, 1994. A new clause (AAA) has been inserted in the said rule to provide that in relation to service provided or agreed to be provided by a person involving an aggregator in any manner, the aggregator of the service would be the person liable for paying service tax.

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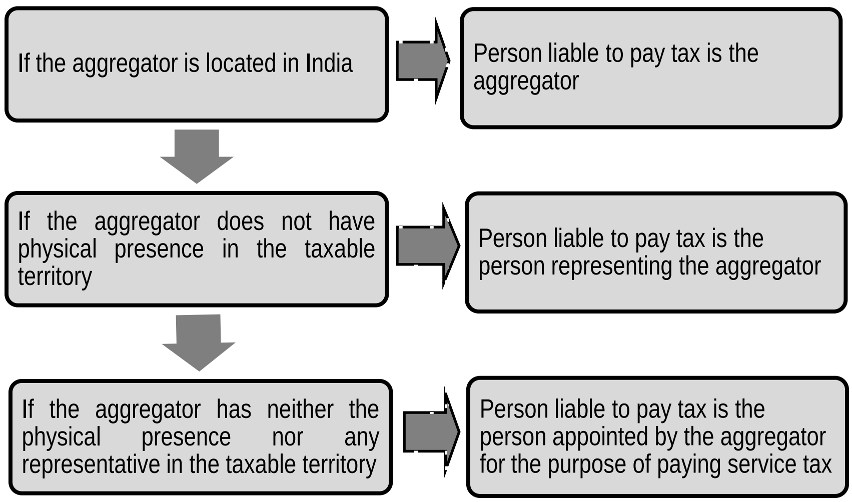
In case, the aggregator does not have a physical presence in the taxable territory, any person representing the aggregator for any purpose in the taxable territory will be liable for paying service tax.

However, if the aggregator neither has a physical presence nor does it have a representative for any purpose in the taxable territory, it will have to appoint a person in the taxable territory for the purpose of paying service tax and such person will be the person liable for paying service tax.

The above has been represented in the diagram given below:



[Effective from 01.03.2015]

(ii) **Service tax to be payable by recipient of service in case of service provided by (a) mutual fund agent/ distributor to mutual fund/ asset management company, (b) selling/marketing agent of lottery tickets to lottery distributor/selling agent [Rule 2(1)(d)(i)(EEA) & Rule 2(1)(d)(i)(EEB)]**

A new clause (EEA) has been inserted in the rule 2(1)(d)(i) to provide that in relation to service provided or agreed to be provided by a mutual fund agent or distributor to a mutual fund or asset management company, the recipient of the service would be the person liable for paying service tax.

A new clause (EEB) has been inserted in the rule 2(1)(d)(i) to provide that in relation to service provided or agreed to be provided by a selling or marketing agent of lottery tickets to a lottery distributor or selling agent, the recipient of the service would be the person liable for paying service tax.

[Effective from 01.04.2015]

(iii) **CBEC to specify conditions, safeguards and procedure for registration in service tax [New sub-rule (9) inserted and sub-rule (1A) omitted in rule 4]**

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CBEC had specified certain documents which were to be submitted by the assessee within a period of 15 days from the date of filing of the application for registration vide the powers given under rule 4(1A).

Sub-rule (1A) has been omitted and a new sub rule (9) inserted to provide that CBEC will, by way of an order, specify the conditions, safeguards and procedure for registration in service tax.

In this regard, *Order No. 1/15 ST dated 28.02.2015, effective from 01.03.2015* has been issued, prescribing documentation, time limits and procedure for registration. It has also been prescribed that henceforth registration for single premises will be granted within two days of filing the application. The Order provides the documentation, time limits and procedure for registration as under:

General procedure

1. Applicants seeking registration for single premises shall file an online application for registration on ACES website in Form ST-1.
2. Following details are to be mandatorily furnished in the application form:
   (a) Permanent Account Number (PAN) of the proprietor or the legal entity being registered (except Government Departments)
   (b) E-mail and mobile number
3. Registration would be granted online within 2 days of filing the complete application form. On grant of registration, the applicant would be enabled to electronically pay service tax.
4. Registration Certificate downloaded from the ACES website would be accepted as proof of registration and there would be no need for a signed copy.

Documentation required

A self attested copy of the following documents will have to be submitted by registered post/ speed post to the concerned Division, within 7 days of filing the Form ST-1 online, for the purposes of verification:

1. Copy of the PAN Card of the proprietor or the legal entity registered
2. Photograph and proof of identity of the person filling the application
3. Document to establish possession of the premises to be registered such as proof of ownership, lease or rent agreement, allotment letter from Government, No Objection Certificate from the legal owner
4. Details of the main Bank Account
5. Memorandum/Articles of Association/List of Directors
6. Authorisation by the Board of Directors/Partners/Proprietor for the person filing the application

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7. Business transaction numbers obtained from other Government departments or agencies such as Customs Registration No. (BIN No), Import Export Code (IEC) number, State Sales Tax Number (VAT), Central Sales Tax Number, Company Index Number (CIN) which have been issued prior to the filing of the service tax registration application

   Verification of premises, if there arises any need for the same, will have to be authorised by an officer not below the rank of Additional/Joint Commissioner.

Revocation of registration certificate

The registration certificate may be revoked by the Deputy/Assistant Commissioner in any of the following situations, after giving the assessee an opportunity to represent against the proposed revocation and taking into consideration the reply received, if any:

1. the premises are found to be non existent or not in possession of the assessee.
2. no documents are received within 15 days of the date of filing the registration application.
3. the documents are found to be incomplete or incorrect in any respect.

[Effective from 01.03.2015]

(iv) Provisions introduced for authentication of invoices by digital signatures [New rule 4C]

A provision has been added for authentication of invoices by means of digital signatures by inserting new rule 4C. New rule 4C provides that any invoice, bill or challan issued under rule 4A or consignment note issued under rule 4B may be authenticated by means of a digital signature. The Board may specify the conditions, safeguards and procedure to be followed by any person issuing digitally signed invoices, by way of a notification.

[Effective from 01.03.2015]

7. Amendments in Reverse Charge Notification

Taxable services in respect of which service tax is payable under section 68(2) of Finance Act, 1994, i.e., under reverse charge are notified under *Notification No. 30/2012 ST dated 20.06.2012.* The said notification has been amended vide ***Notification No. 7/2015 ST dated 01.03.2015*** as under:

(i) 100% service tax to be paid under reverse charge in case of service provided by (a) mutual fund agent/ distributor to mutual fund/ asset management company, (b) selling/marketing agent of lottery tickets to lottery distributor/selling agent and (c) person involving an aggregator

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Following services have been added in the list of services on which service tax is payable under full reverse charge (100% service tax to be paid by the person liable for paying service tax other than the service provider):

(a) Taxable services provided or agreed to be provided by a mutual fund agent or distributor, to a mutual fund or asset management company - *Effective from 01.04.2015*

(b) Taxable services provided or agreed to be provided by a selling or marketing agent of lottery tickets to a lottery distributor or selling agent - *Effective from 01.04.2015*

(c) Taxable services provided or agreed to be provided by a person involving an aggregator in any manner - *Effective from 01.03.2015*

(ii) Scope of reverse charge widened

The scope of reverse charge provisions has been widened with the introduction of concept of aggregator under service tax. Earlier, service tax was payable either by the service provider (normal charge) or the service receiver (reverse charge – full or partial). However, now under reverse charge provisions, service tax may be payable by any other person (who is liable for paying service tax) who may or may not be the service receiver e.g., an aggregator). Thus, an amendment has been made in paragraph II of the notification to give effect to this amendment.

Further, in the Table in column (4), the column heading "percentage of service tax payable by the person receiving the service" has been substituted with "percentage of service tax payable by any person liable for paying service tax other than the service provider" as person liable to pay service tax may not necessarily be service receiver.

[Effective from 01.03.2015]

(iii) Entire service tax to be paid under reverse charge in case of manpower supply and security services

Earlier, in respect of services provided or agreed to be provided by way of supply of manpower for any purpose or security services by any individual, HUF or partnership firm including association of persons to a business entity registered as body corporate, 25% of service tax was payable by the person providing the service and remaining 75% by the service receiver.

However, now the entire service tax i.e., 100% service tax would be payable by the person liable for paying service tax other than the service provider (service recipient in this case).

[Effective from 01.04.2015]

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CENVAT credit

1. Following amendments have been made in CENVAT Credit Rules, 2004 [CCR] vide *Notification No. 6/2015 CE (NT) dated 01.03.2015*:

   (i) **CENVAT credit allowed on inputs and capital goods received directly in the premises of the job worker [Rules 4(1) and 4(2)(a)]**

   Earlier, rule 4(1) allowed instant CENVAT credit on receipt of inputs into the factory of the manufacturer or in the premises of the output service provider or on the delivery of inputs to the output service provider. Likewise, rule 4(2)(a) allowed CENVAT credit on capital goods on receipt of the same in the factory or in the premises of the output service provider or outside the factory for generation of electricity for captive use within the factory or on the delivery of capital goods to the output service provider. Further, when goods were directly sent to job-worker's premises without bringing them in the manufacturer/output service provider's premises, CENVAT credit could be taken only when such goods were received back from the job-worker's premises in the premises of manufacturer/output service provider.

   Rule 4(1) and rule 4(2)(a) have been amended to allow CENVAT credit in respect of inputs and capital goods immediately on receipt of the same in the premises of job worker where the same are sent directly to the job worker on the direction of the manufacturer or the provider of output service, as the case may be.

   [Effective from 01.03.2015]

   (ii) **Time limit for availing credit on inputs and input services increased from 6 months to 1 year of the date of invoice [Rules 4(1) and 4(7)]**

   The time limit for availment of CENVAT credit on inputs and input services has been extended from six months to one year of the date of the issue of invoice/bill/challan etc. Amendments have been made in third proviso to rule 4(1) and the erstwhile sixth proviso (now fifth proviso) to rule 4(7) to enhance the time limit for availability of credit in respect of inputs and input services respectively.

   The provisos lay down that the manufacturer and the provider of output service shall not take CENVAT credit after one year of the date of issue of any of the documents specified in rule 9(1).

   [Effective from 01.03.2015]

   (iii) **Time limit for return of capital goods from a job worker to manufacturer/output service provider increased from 6 months to 2 years [Rule 4(5)]**

   Earlier, rule 4(5)(a) *inter alia* provided for a common time limit of 180 days for return of inputs and capital goods sent to a job-worker for the purpose of availing CENVAT credit.

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Rule 4(5)(a) has now been amended to provide as follows:-

(a) CENVAT credit on inputs will be allowed even if any inputs as such or after being partially processed are sent to a job worker and from there subsequently sent to another job worker and likewise, for

- further processing,
- testing,
- repairing,
- re-conditioning or
- for the manufacture of intermediate goods necessary for the manufacture of final products or
- any other purpose.

Such credit will be allowed only if it is established from the records /challans/ memos/ or any other document produced by the manufacturer/ output service provider taking CENVAT credit that the inputs or the products produced therefrom are received back by the manufacturer/ output service provider within 180 days of their being sent from the factory/premises of output service provider, as the case may be.

(b) CENVAT credit on capital goods will be allowed even if any capital goods as such are sent to a job worker for

- further processing,
- testing,
- repair,
- re-conditioning or
- for the manufacture of intermediate goods necessary for the manufacture of final products or
- any other purpose.

Such credit will be allowed only if it is established from the records, challans or memos or any other document produced by the manufacturer /output service provider taking the CENVAT credit that the capital goods are received back by the manufacturer /output service provider, as the case may be, within 2 years of their being so sent.

(c) Further, the credit will be allowed even if any inputs or capital goods are directly sent to a job worker without their being first brought to the premises of the manufacturer/ output service provider and in such a case, the period of 180 days or 2 years, as the case may be, will be counted from the date of receipt of such goods by the job worker.

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(d) If the inputs or capital goods are not received back within 180 days and 2 years respectively, the manufacturer/ output service provider will have to pay an amount equivalent to the CENVAT credit attributable to the inputs or capital goods by debiting the CENVAT credit or otherwise. However, such credit may be retaken once the inputs or capital goods are received back in the factory/ premises of the output service provider.

[Effective from 01.03.2015]

(iv) **Provisions relating to availment of CENVAT credit under partial and full reverse charge brought at par [Rule 4(7)]**

Prior to 01.04.2015, there were separate provisions for availment of credit on input services in case of payment of service tax under full reverse charge and partial reverse charge. Whereas under full reverse charge, payment of service tax ensured availability of credit on input services; under partial reverse charge, payment to service provider (along with payment of service tax) was also a pre-requisite for availing credit.

The provisions for availing credit of service tax paid under partial reverse charge have now been aligned with the provisions applicable for full reverse charge. Thus, now CENVAT credit of service tax paid under partial reverse charge by the service receiver will also be allowed on payment of service tax alone without linking it to the payment to the service provider. The second proviso has been omitted and first proviso to rule 4(7) amended to give effect to this amendment.

Earlier, the third proviso to rule 4(7) laid down that CENVAT credit availed on input service ought to be reversed (except in case where service tax has been paid under full reverse charge) if value of input service and service tax is not paid within three months of the date of the invoice/bill/challan. The amount equivalent to the credit reversed could be taken back whenever the payment of value of input service and service tax is made.

The provisions contained in the erstwhile third proviso have now been set out in new second proviso to sub-rule (7). Cases where service tax is paid under reverse charge (both partial or full) have been excluded in the newly inserted second proviso.

[Effective from 01.04.2015]

(v) **Explanations (I) and (II) to sub-rule (7) of rule 4 to apply to entire rule 4**

Earlier, the below mentioned explanations were only applicable to sub-rule (7) of rule 4:

"I. The amount mentioned in this sub-rule shall be paid by the manufacturer of goods or the provider of output service by debiting the CENVAT credit or otherwise on or before the 5th day of the following month except for the month

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of March, when such payment shall be made on or before the 31st day of the month of March.

II. *If the manufacturer of goods or the provider of output service fails to pay the amount payable under this* **sub-rule**, *it shall be recovered, in the manner as provided in rule 14, for recovery of CENVAT credit wrongly taken."*

However, now the above-mentioned explanations have been made applicable to entire rule 4 by substituting the words '**sub-rule**' appearing therein with the word '**rule'**.

Thus, in effect, earlier the two explanations were applicable in respect of amount payable on non-payment of value of input service and service tax within three months of date of invoice as provided under sub-rule (7). However, now they will also apply in relation to amount payable on non-receipt of inputs and capital goods within 180 days and 2 years respectively under sub-rule (5)(a)(iii).

[Effective from 01.03.2015]

(vi) **Export goods defined for the purpose of refund of CENVAT credit under rule 5 [Clause (1A) of Explanation 1 to rule 5]**

Rule 5 provides for refund of CENVAT credit when a manufacturer clears export goods without payment of duty or a service provider exports an output service without payment of service tax. Refund is computed as per the formula prescribed in the rule and is subject to certain procedure, safeguards, conditions and limitations specified by the Board.

Though the term 'export service' has been defined in the rule, the term 'export goods' was not defined in the rule. The definition of 'export goods' has now been inserted in the rule to mean any goods which are to be taken out of India to a place outside India. Clause (1A) has been inserted in Explanation 1 to rule 5 to give effect to this amendment.

[Effective from 01.03.2015]

(vii) **Inputs and input services used in the manufacture of non-excisable goods to attract reversal provisions under rule 6 [Explanations (1) and (2) to rule 6(1)]**

(a) Rule 6 lays down the provisions for reversal of CENVAT credit when a manufacturer manufactures both dutiable and exempted final products or a service provider provides both taxable and exempted services.

(b) The rule sets out the various options to quantify the credit that needs to be reversed on inputs and input services which are used in manufacture of exempted goods or in provision of exempted services.

(c) Under rule 2(d) of CCR, **exempted goods are defined as excisable goods** which are exempt from the whole of the duty of excise leviable thereon, and

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includes goods which are chargeable to "Nil" rate of duty and goods in respect of which the benefit of an exemption under *Notification No. 1/2011 C.E. dated 01.03.2011* or under entries at serial numbers 67 and 128 of *Notification No. 12/2012 C.E. dated 17.03.2012* is availed.

(d) However, it has now been clarified vide Explanation 1 inserted after sub-rule (1) that for the purposes of this rule, exempted goods or final products as defined in clauses (d) and (h) of rule 2 will include non-excisable goods cleared for a consideration from the factory.

(e) It has been further clarified vide Explanation 2 that value of non –excisable goods for the purpose of this rule, will be the invoice value. Where such invoice value would not be available, the value will be determined by using reasonable means consistent with the principles of valuation contained in the Excise Act and the rules made thereunder.

(f) It is to be noted that the above explanations are applicable only to rule 6.

(g) The implication of the said amendment is that inputs and input services used in the manufacture of non-excisable goods will also attract the reversal provisions under rule 6. To illustrate, if a manufacturer manufactures dutiable and non-excisable goods, credit on input or input services used in the manufacture of non-excisable goods will have to be reversed in accordance with the provisions of rule 6.

(h) It is worthwhile to note here that since exempted service *inter alia* means services on which no service tax is leviable under section 66B of Finance Act, 1994, credit of inputs or input services used in provision of non-taxable services is required to be reversed under rule 6.

(i) Thus, now after the amendment in rule 6, there remains no difference with regard to reversal of credit by a manufacturer *vis-a-vis* a service provider. In other words, provisions for reversal of credit on exempted goods and exempted services have now been aligned.

[Effective from 01.03.2015]

(viii) Provisions applicable to first/second stage dealer regarding maintenance of records to be able to pass on the credit, to apply to an importer issuing CENVATable invoice [Rule 9(4)]

Rule 9(4) provides that CENVAT credit in respect of input or capital goods purchased from a first stage dealer or second stage dealer will be allowed only if such first stage dealer or second stage dealer has maintained records indicating the fact that the input or capital goods was supplied from the stock on which duty was paid by the producer of such input or capital goods and only an amount of such duty on *pro rata* basis has been indicated in the invoice issued by him.

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A proviso has been inserted in the sub-rule (4) which lays down that provisions of this sub-rule will apply *mutatis mutandis* to an importer who issues an invoice on which CENVAT credit can be taken.

[Effective from 01.03.2015]

2. **Clarification regarding availment of CENVAT credit after six months (now one year)**

It has been clarified by CBEC that the limitation period of 6 months for availing CENVAT credit would not apply when re-credit is taken of amount reversed under:

(i) third proviso (now second proviso) to rule 4(7) of the CENVAT Credit Rules, 2004 (CCR)

(ii) rule 3(5B) of CCR

(iii) rule 4(5)(a) of CCR,

after meeting the conditions prescribed in these rules. The limitation period of 6 months applies only when the credit is taken for the first time on an eligible document.

[Circular No. 990/14/2014 CX dated 19.11.2014]

Note: *This Circular was issued during the period when the limitation period for availment of CENVAT credit was 6 months. However, the principle on the basis of which the clarification is issued will apply under new limitation period of 1 year also. Thus, the Circular may apply for amended provisions also.*

Third proviso to rule 4(7) (now second proviso), rule 3(5B) and rule 4(5)(a) of CCR stipulate as follows:

(i) ***Third proviso to rule 4(7) of CCR*** *(now second proviso) prescribes that if the payment of value of input service and service tax payable is not made within three months of date of invoice, bill or challan, then the CENVAT credit availed is required to be paid back by the manufacturer or service provider. Subsequently, when such payment of value of input service and service tax is made, the amount so paid back can be re-credited.*

(ii) ***Rule 3(5B) of CCR*** *stipulates that if the value of any input or capital goods before being put to use on which CENVAT credit has been taken, is written off or such provisions made in Books of Account, the manufacturer or service provider is required to pay an amount equal to credit so taken. However, when the inputs or capital goods are subsequently used, the amount so paid can be re-credited in the account.*

(iii) ***Rule 4(5)(a) of CCR*** *prescribes that in case inputs/capital goods sent to job worker are not received back within 180 days/ 2 years, the manufacturer or service provider is required to pay an amount equal to credit taken on such inputs/ capital goods in the first instance. However, when the inputs/ capital goods are subsequently received back from job worker, credit can be retaken of the amount so paid.*

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3. **Clarification regarding determination of place of removal in the case of exports for purposes of CENVAT credit of input services**

While determining the eligibility of the input services to CENVAT credit, determination of place of removal is required. The following has been clarified in this regard:

(i) Place of removal in case of direct export of goods by the manufacturer exporter to his foreign buyer will be the port/ICD/CFS where the shipping bill is filed by the manufacturer exporter.

(ii) Place of removal in case of clearance of goods from the factory for export by a merchant exporter will be the factory gate. However, in isolated cases, it may extend further also depending on the facts of the case, but in no case, this place can be beyond the Port/ ICD/CFS where shipping bill is filed by the merchant exporter.

[Circular No. 999/6/2015 CX dated 28.02.2015]

PART – II: QUESTIONS AND ANSWERS

QUESTIONS

Note: Questions have to be answered on the basis of position of law as amended by the Finance (No. 2) Act, 2014 and significant notifications/circulars issued till 30.04.2015.

Residential Status and Scope of total income

1. Miss Rosy, a Canadian national, got married to Mr. Ankur of India in Canada on 4.02.2014 and came to India for the first time on 16.03.2014. She remained in India up till 15.9.2014 and left for Canada on 16.9.2014. She returned to India again on 22.03.2015. While in India, she had purchased a shop in Pune on 25.04.2014, which was let-out to a company on a rent of ₹ 50,000 p.m. from 1.06.2014. She had taken loan from a bank for purchase of this shop on which bank had charged interest of ₹ 1,25,000 upto 31.03.2015. She had received the following gifts from her relatives and friends during 1.4.2014 to 15.9.2014:

-	From parents of husband	₹ 51,000
-	From married sister of husband	₹ 21,000
-	From two very close friends of her husband,	₹ 75,000 and ₹ 50,000.

Determine her residential status and compute the total income chargeable to tax along with the amount of tax payable on such income for the Assessment Year 2015-16.

Income which do not form part of total income

2. State, with reasons in brief, whether the following statements are true or false with reference to the provisions of the Income-tax Act, 1961:

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(i) Mr. Arun, a member of a HUF, received ₹ 50,000 as his share from the income of the HUF. The same is to be included in his total income.

(ii) A public charitable trust registered under section 12AA, running a hospital has claimed the cost of a laptops (acquired for hospital on 23.03.2014) amounting to ₹1,20,000 as application of income for the P.Y.2013-14. It can also claim depreciation @ 60% thereon for P.Y. 2014-15, as deduction while computing income for the purpose of application.

(iii) Ramji charitable trust, registered under section 12AA, earned income from mutual funds specified under section 10(23D) to the tune of ₹ 2 lakh in the P.Y. 2014-15 and claims exemption under section 10(35) in respect of such income. It also earned dividend income of ₹ 1 lakh and agricultural income of ₹ 5 lakh in the same year, and claims exemption under section 10(34) and 10(1), respectively, in respect of such income, without complying with the conditions laid down under section 11. All the three claims for exemption under section 10 are tenable.

(iv) Agricultural income from a land situated in Malaysia would be taxable in the hands of Mr. Anand, a resident in India.

(v) Mr. X is a 'Maha Vir Chakra' awardee who was in the service of the Central Government. Pension of ₹ 3,50,000 received by him during the financial year 2014-15 is chargeable to tax in his hands.

Salaries

3. (a) From the following details, find out the salary income chargeable to tax in the hands of Mr. Vansh for the assessment year 2015-16:

Mr. Vansh is a regular employee of X Ltd. in Delhi. He was appointed on 01-03-2014 in the scale of 27,000-3200-35,000. He is paid dearness allowance (which forms part of salary for retirement benefits)@30% of basic pay and bonus equivalent to one and a half month's basic pay as at the end of the year. He contributes 18% of his salary (basic pay plus dearness allowance) towards recognized provident fund and the company contributes the same amount.

He is provided free housing facility which has been taken on rent by the company at ₹ 18,000 per month. He is also provided with following facilities:

(i) The company reimbursed the medical treatment bill of ₹ 43,000 of his daughter, who is dependent on him.

(ii) The monthly salary of ₹ 5,600 of a house keeper is reimbursed by the company.

(iii) He is getting telephone allowance of ₹ 1,200 per month.

(iv) A gift voucher of ₹ 4,900 was given on the occasion of his marriage anniversary.

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(v) The company pays medical insurance premium to effect an insurance on the health of Mr. Vansh ₹ 10,500.

(vi) Motor car running and maintenance charges of ₹ 48,200 fully paid by employer. (The motor car is owned and driven by Mr. Vansh. The engine cubic capacity is below 1.60 litres. The motor car is used for both official and personal purpose by the employee.)

(vii) Value of free lunch provided during office hours is ₹ 1,000.

(viii) Facility of laptop and computer was provided to Mr. Vansh both for official and personal use. The cost of laptop and computer acquired by the company on 01.12.2014, are ₹ 45,000 and ₹ 35,000, respectively.

(ix) Professional tax paid ₹ 3,000, of which ₹ 2,000 was paid by the employer.

(b) Mr. Satvik is employed with MN Ltd. on a basic salary of ₹ 12,000 p.m. He is also entitled to dearness allowance @ 100% of basic salary, 50% of which is included in salary as per terms of employment. The company gives him house rent allowance of ₹ 6,600 p.m. which was increased to ₹ 7,200 p.m. with effect from 1.01.2015. He also got an increment of ₹ 1,200 p.m. in his basic salary with effect from 1.02.2015. Rent paid by him during the previous year 2014-15 is as under:

April and May, 2014	Nil, as he stayed with his parents
June to October, 2014	₹ 6,500 p.m. for an accommodation in Gurgaon
November, 2014 to March, 2015	₹ 8,500 p.m. for an accommodation in Noida.

Compute his gross salary for assessment year 2015-16.

Income from house property

4. Ronak owns a house in Bangalore. During the previous year 2014-15, 2/3rd portion of the house was self-occupied and 1/3rd portion was let out for residential purposes at a rent of ₹ 9,200 p.m. Municipal value of the property is ₹ 3,30,000 p.a., fair rent is ₹ 3,00,000 p.a. and standard rent is ₹ 3,60,000. He paid municipal taxes @10% of municipal value during the year. A loan of ₹ 38,00,000 was taken by him during the year 2012 for acquiring the property. Interest on loan paid during the previous year 2014-15 was ₹ 3,90,000. Compute Ronak's income from house property for the A.Y.2015-16.

Profits and gains of business or profession

5. Mr. Prabhakar commenced operations of the businesses of setting up a warehousing facility for storage of food grains, sugar and edible oil on 1.4.2014. He incurred capital expenditure of ₹ 70 lakh, ₹ 50 lakh and ₹ 40 lakh, respectively, on purchase of land and building during the period November, 2013 to March, 2014 exclusively for the above businesses, and capitalized the same in its books of account as on 1st April, 2014. The cost of land included in the above figures are ₹ 40 lakh, ₹ 30 lakh and ₹ 20 lakh, respectively. Further, during the P.Y.2014-15, it incurred capital expenditure of ₹ 15 lakh,

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₹ 10 lakh & ₹ 8 lakh, respectively, for extension/reconstruction of the building purchased and used exclusively for the above businesses.

The profits from the business of setting up a warehousing facility for storage of food grains, sugar and edible oil (before claiming deduction under section 35AD and section 32) for the A.Y. 2015-16 are ₹ 15 lakhs, ₹ 13 lakhs and ₹ 29 lakhs, respectively

Compute the income under the head "Profits and gains of business or profession" for the A.Y.2015-16 and the loss to be carried forward, assuming that Mr. Prabhakar has fulfilled all the conditions specified for claim of deduction under section 35AD and has not claimed any deduction under Chapter VI-A under the heading "C. – Deductions in respect of certain incomes".

Capital Gains

6. Mr. Jaiprakash inherited a house in Aligarh under will of his father in October, 2003. The house was purchased by his father in August, 1979 for ₹ 8,25,000. He invested an amount of ₹ 10,50,000 in construction of one more floor in this house in July, 2005.

   He decided to sell the property to Mr. Suresh for ₹ 65,00,000 and received an advance of ₹ 6,50,000 in May 2009. Mr. Suresh was unable to pay the balance amount and hence, the entire advance was forfeited by Mr. Jaiprakash.

   Again Mr. Jaiprakash entered into an agreement to sell the property to Mr. Mahesh for ₹ 70,00,000 and received advance money of ₹ 7,00,000 in June, 2014. But again the transfer did not materialise due to which the advance money was again forfeited.

   The house was finally sold by him in November, 2014 for ₹ 85,50,000 to Mr. Dinesh. The valuation adopted by the registration authorities for charge of stamp duty was ₹ 95,25,000 which was not contested by the buyer, but as per assessee's request, the Assessing Officer made a reference to Valuation Officer. The value determined by the Valuation officer was ₹ 98,00,000. Brokerage@1% of sale consideration was paid by Mr. Jaiprakash to the agent. The fair market value of house as on 01.04.1981 was ₹ 8,30,000.

   He invested ₹ 30,00,000 in 3 years bonds of NHAI in January 2015 and ₹ 35,00,000 in 3 years bonds of RECL in April 2015, out of the net consideration arising on sale of residential house.

   You are required to compute the gross total income of Mr. Jaiprakash for A.Y. 2015-16 with the help of the given information and by taking CII for the F.Y. 2003-04 : 463, F.Y. 2005-06: 497, F.Y. 2009-10: 632 and for F.Y. 2014-15:1024.

Income from Other Sources

7. State whether the following are chargeable to tax and the amount liable to tax in each case:

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(i) A sum of ₹ 2,15,000 was received as gift from non-relatives by Mr. Ranu on the occasion of the marriage of his son Sahil.

(ii) A wrist watch worth ₹ 52,000 is received by Sarthak from his friend on his 25th Birthday.

(iii) Ms. Runjhun received a cash gift of ₹ 51,000 from elder brother of her husband's grandfather on 01.08.2014.

(iv) Interest on enhanced compensation of ₹ 1,75,000 received on 14-8-2014 for acquisition of urban land, of which 60% relates to the earlier year.

Income of Other Persons included in Assessee's Total Income

8. Examine the correctness or otherwise of the claims made in the following cases:

(i) Aarav who is a physically handicapped minor (suffering from a disability of the nature specified in section 80U), earns bank interest of ₹ 85,000 and ₹ 90,000 from making bags manually by himself.

Aarav's father claims that such income shall not be included in his hands but shall be computed in the hands of Aarav separately.

(ii) Mrs. Parvati transferred her immovable property to her friend Mr. Harsh without consideration, subject to a condition that out of the rental income from such property, a sum of ₹ 38,000 per annum shall be credited to her daughter-in-law's bank account.

Mrs. Parvati claims that the amount of ₹ 38,000 (utilized by her son's wife) should not be included in her total income as she no longer owned the property.

Set off and Carry Forward of Losses

9. Mr. Aaditya submits the following information for the financial year ending 31st March, 2015. He desires that you should:

(a) Compute his total income and

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

	Particulars	₹
(i)	He has two houses :	
	(a) House No. I – Income after all statutory deductions	84,000
	(b) House No. II – Current year loss	(56,000)
(ii)	He has four proprietary businesses :	
	(a) Textile Business :	
	(i) Discontinued from 31st October, 2014 – Current year loss	60,000
	(ii) Brought forward business loss of A.Y.2011-12	1,05,000

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	(b)	Chemical Business :	
		(i) Discontinued from 1st March, 2013 – hence no profit/loss	Nil
		(ii) Bad debts allowed in earlier years recovered during this year	38,000
		(iii) Brought forward business loss of A.Y. 2013-14	55,000
	(c)	Leather Business : Profit for the current year	2,50,000
	(d)	Loss from specified business under section 35AD	80,000
	(e)	Share of profit in a firm in which he is partner since 2003	21,050
(iii)	(a)	Short-term capital gain	65,000
	(b)	Long-term capital loss	42,000
(iv)	LIC premium paid		18,000

Deductions from Gross Total Income

10. For the Assessment year 2015-16, the gross total income of Mr. Shivpal, a resident in India, was ₹ 9,25,600 which includes long-term capital gain of ₹ 3,15,000 and short-term capital gain under section 111A of ₹64,500. The gross total income also includes interest income of ₹ 13,500 from savings bank deposits with banks. Mr. Shivpal has invested in PPF ₹ 1,50,000 and also paid a medical insurance premium ₹ 24,000 to insure his health. Mr. Shivpal also contributed ₹ 68,000 to public charitable trust eligible for deduction under section 80G by way of an account payee cheque. Compute the total income and tax thereon of Mr. Shivpal, who is 72 years old as on 31.3.2015.

Computation of Total Income of an individual

11. Mr. Yashwant carries on his own business. An analysis of his trading and profit & loss for the year ended 31-3-2015 revealed the following information:

    (1) The net profit was ₹ 13,47,000.

    (2) The following incomes were credited in the profit and loss account :

    (a) Income from UTI ₹ 28,000.

    (b) Interest on debentures (Gross) ₹ 34,200.

    (c) Winnings from races (net of TDS) ₹ 33,600.

    (3) It was found that some stocks were omitted to be included in both the opening and closing stocks, the value of which were:

    Opening stock ₹ 10,500.

    Closing stock ₹ 14,000.

    (4) ₹ 1,25,000 was debited in the profit and loss account, being contribution to a University approved and notified under section 35(1)(ii).

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(5) Salary includes ₹ 27,000 paid to his brother which is unreasonable to the extent of ₹ 5,000.

(6) Advertisement expenses include 20 gift packets of dry fruits costing ₹ 1,250 per packet presented to important customers.

(7) Total expenses on car was ₹ 95,000. The car was used both for business and personal purposes. ¾th is for business purposes.

(8) Miscellaneous expenses included ₹33,500 paid to Shiva & Co., a goods transport operator in cash on 28-2-2015 for distribution of the company's product to the warehouses.

(9) Depreciation debited in the books was ₹ 95,000. Depreciation allowed as per Income-tax Rules, 1962 was ₹ 82,000.

(10) Drawings ₹ 18,000.

(11) Investment in NSC ₹ 27,000.

Compute the total income of Mr. Yashwant for the assessment year 2015-16.

Provisions concerning deduction of tax at source

12. Examine the applicability of the provisions for tax deduction at source in the following cases -

(i) On 12.02.2015, payment of ₹ 2,20,000 made to Mr. Arvind for purchase of diaries made according to specifications of M/s Sutra Ltd. However, no material was supplied for such diaries to Mr. Arvind by M/s Sutra Ltd.

(ii) Mr. Mohit sold his house property in Ranchi as well as rural agricultural land for a consideration of ₹ 68,00,000 and ₹ 27,00,000, respectively, to Mr. Rajesh on 01.12.2014.

(iii) Miss Sonia, a resident, is due to receive ₹ 2,30,000 on 31.10.2014 on maturity of her life insurance policy taken 01.11.2010. The policy sum assured is ₹ 2,00,000 and the annual premium is ₹ 45,000.

(iv) Rent of ₹ 1,75,000 paid for hire of plant and machinery by a partnership firm.

(v) Compensation of ₹ 2,00,000 paid to Mr. Devesh for compulsory acquisition of his urban land by the State Government.

Provisions for filing of Return of Income

13. State with reasons, whether the following statements are true or false, with regard to the provisions of the Income-tax Act, 1961:

(i) Return of income of Limited Liability Partnership (LLP) can be verified by any partner.

(ii) An individual, who is not in India, can verify the return of income from outside India.

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Computation of Assessable Value under Central Excise

14. Spring Fresh is a leading manufacturer of bottled aerated water. Legal Metrology Act, 2009 requires declaration of retail sale price on the bottles of aerated water.

Following information has been furnished by Spring Fresh:

Particulars	Amount (₹)
Abatement available on aerated water - 40% of retail sale price	
MRP marked on the bottles of aerated water	₹ 30 per bottle
Price at which Spring Fresh sells the bottles of aerated water to their wholesalers	₹ 19 per bottle
Price at which wholesalers sell the bottles of aerated water to retail shop owners	₹ 24 per bottle
Price at which bottles of aerated water are sold by retailers to final consumers	₹ 28 per bottle (₹ 2 offered as discount on printed MRP)

Calculate the assessable value for the purpose of excise duty on the bottles of aerated water. Will your answer change, if Spring Fresh declares two MRPs namely, ₹ 30 and ₹ 40 on each bottle of aerated water?

Note: Aerated waters are notified under section 4A of Central Excise Act, 1944 (RSP based valuation provisions).

Computation of Customs Duty

15. Mahabalipur Enterprises imported some goods in a vessel. The assessable value of the imported goods is ₹ 10,00,000. Compute the customs duty payable from the following additional information:

Date of bill of entry	09.10.2014 (Rate of BCD is 8%)
Date of entry inwards	19.10.2014 (Rate of BCD is 10%)
CVD is payable @ 12%	
Special CVD – as applicable	

Will your answer change if the goods are imported in a vehicle?

CST Liability

16. Mr. Harish is a registered dealer in Delhi. You are required to compute the central sales-tax payable by him from the details furnished below:-

Particulars	₹
Total inter-State sales (including CST)	16,00,000

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(i)	Weighment dues (Weighing is incidental to the goods being sold)	48,000
(ii)	Deposits for returnable container	25,000
(iii)	Excise duty	80,000
(iv)	Freight charges recovered separately in the invoice	60,000
(v)	Goods returned by dealers within six months of sale, but after the end of the financial year	40,000
Amounts given in points (i) to (v) above are included in total inter-State sales of ₹ 16,00,000		
Buyers have issued ‘C’ forms for all purchases		
Sales tax rate within the State is 1%.		

Input Tax Credit

17. Sparsh Enterprises, a dealer in consumer goods, submits the following information pertaining to the month of December, 2014:

    (i) Exempt goods 'P' purchased for ₹ 1,75,000 and sold for ₹ 3,50,000.

    (ii) Goods 'Q' purchased for ₹ 2,25,000 (including VAT) and sold at a margin of 20% profit on purchases (VAT rate for purchases and sales 12.5%)

    (iii) Goods 'R' purchased for ₹ 2,00,000 (excluding VAT) and sold for ₹ 2,50,000 (VAT rate for purchases and sales 4%);

    (iv) His unutilized balance of input VAT credit on 1.12.2014 was ₹ 3,000.

    Compute the turnover, Input VAT, Output VAT and Net VAT payable by Sparsh Enterprises.

Basic Concepts of Service Tax

18. With reference to the provisions of service tax law, briefly examine the service tax implications in the following independent cases:-

    (a) Miss Chaitali is working as an Assistant Manager in Success Software Limited (SSL) since 01.04.2013. One of the clause of her employment contract provides that she would be given one month notice by SSL in the event of termination of her services by SSL. However, she has been terminated all of a sudden on 31.3.2015 on account of her poor performance. She was paid termination compensation of ₹ 1,25,0000.

    (b) Mr. Deepak Jindal has entered into a contract with High Technologies Ltd. for rendering legal consultancy services for one year on a lumpsum fee of ₹ 1,25,000 per month.

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Point of Taxation

19. With reference to Point of Taxation Rules, 2011, determine the point of taxation in respect of following independent transactions:

    (a) MNO Ltd. paid directors' fee of ₹ 1,00,000 to one of its director for attending a Board Meeting held in the month of December. The meeting was held for approving accounts of the company. Though the journal entry for the transaction was passed on the same day, actual payment was made to the director by the end of April.

    (b) PQR Ltd. paid consultancy fees of ₹ 50,000 to its associated enterprises located in Dubai. Dubai firm raised the invoice on 27.01.2015 and the same was received by PQR Ltd. on 06.02.2015. Though the journal entry was passed on 07.02.2015 in the books of PQR Ltd., actual payment to Dubai firm was made on 25.02.2015.

Valuation of Taxable Service

20. Krishna, an interior decorator, designed the interiors of Mr. P's newly set up office in Navi Mumbai. As a consideration for the said services, Mr. P gave a souvenir to Krishna. The said souvenir was an artefact especially designed and made by the craftsmen as per the specifications suggested by Mr. P.

    Krishna did not pay service tax on the services provided by him contending that value thereof could not be ascertained. Is Krishna's contention correct? Critically examine the case assuming that Krishna is not entitled to avail small service providers' exemption under *Notification No. 33/2012 ST dated 20.06.2012*.

Liability of Aggregator under Service Tax

21. Mr. X, a Delhi resident, submits a cab request to Speed Cabs for travelling from Delhi to Gurgaon. Speed Cabs is a mobile application owned and managed by Speed Technologies Ltd. located in India. The application facilitates a potential customer to connect with persons providing cab service under the brand name of Speed Cabs. After Mr. X pays the cab charges using his debit card, he gets details of the driver, Mr. Y and the cab's registration number.

    With reference to the Service Tax Rules, 1994, discuss who is liable to pay service tax in this case. Will your answer be different, if Speed Technologies Ltd. is located in New York and does not have a representative in India?

Exemption, Abatement and Reverse Charge under Service Tax

22. Briefly answer the following questions:-

    (i) Armaan travelled by air in business class on 15.04.2015, by Origin Airlines. He booked the ticket on the same day. The airfare charges (value on which service tax was payable) was ₹ 1,00,000. Determine the amount of service tax payable on the service received by Armaan assuming that:

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(a) Origin Airlines opted for abatement under *Notification No. 26/2012 ST dated 20.06.2012* and did not avail CENVAT credit on inputs and capital goods used for providing such service,

(b) Rate of service tax is 12% and education cess is 3%, and

(c) Origin Airlines is not eligible for small service provider's exemption under *Notification No. 33/2012 ST dated 20.06.2012.*

(ii) Raghav, a mutual fund agent, provided services to ABC Asset Management Company Ltd. on 20.04.2015. Raghav is of the view that services provided by him are exempted as per the Mega Exemption *Notification No. 25/2012 ST dated 20.06.2012.*

Examine whether Raghav's view is correct and if not, discuss the correct legal position in the given case.

Late fee for Delayed Return under Service Tax

23. Fitness Ltd. is engaged in providing taxable services for the half year ended on 30th September, 2014. The company filed its service tax return on:

Case I: 9th November, 2014

Case II: 23rd November, 2014

Case III: 25th January, 2015

Determine the amount of late fee payable, if any, by Fitness Ltd. in each of the above independent cases.

CENVAT Credit

24. Examine whether the following purchases are eligible for CENVAT credit as capital goods under rule 2(a) of CENVAT Credit Rules, 2004.

(i) Safe Cabs Limited, engaged in providing passenger carriage service, purchased 3 new cars (in the name of its associate and registered as such) for their business.

(ii) King Riders, engaged in the manufacture of excisable goods purchased two special purpose vehicles falling under Tariff Heading 8705 for use in its factory.

25. Briefly answer the following questions with reference to the provisions of CENVAT Credit Rules, 2004:-

(i) Mr. Q, a manufacturer, receives an invoice dated 05.03.2015 for inputs purchased by it. Mr. Q has been advised by his consultant that CENVAT credit on said inputs cannot be taken after six months of the date of invoice. You are required to offer your comments, if any.

(ii) Mr. P, an output service provider, receives some capital goods within his premises and immediately sends them to a job worker for reconditioning on 22.03.2015. Mr. P has been informed by his consultant that for the purpose of availing CENVAT

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credit, he should get back the capital goods in his premises within 180 days of their being sent from his premises.

SUGGESTED ANSWERS / HINTS

1. Under section 6(1), an individual is said to be resident in India in any previous year, if he satisfies any one of the following conditions:

   (i) He has been in India during the previous year for a total period of 182 days or more, or

   (ii) He has been in India during the 4 years immediately preceding the previous year for a total period of 365 days or more and has been in India for at least 60 days in the previous year.

   If an individual satisfies any one of the conditions mentioned above, he is a resident. If both the above conditions are not satisfied, the individual is a non-resident.

   Therefore, the residential status of Miss Rosy, a Canadian, for A.Y.2015-16 has to be determined on the basis of her stay in India during the previous year relevant to A.Y. 2015-16 i.e., P.Y.2014-15 and in the preceding four assessment years.

   Her stay in India during the previous year 2014-15 and in the preceding four years are as under:

   P.Y.2014-15

01.04.2014 to 15.09.2014	-	168 days
22.03.2015 to 31.03.2015	-	10 days
Total		178 days

   Four preceding previous years

P.Y.2013-14 [1.4.2013 to 31.3.2014]	-	16 days
P.Y.2012-13 [1.4.2012 to 31.3.2013]	-	Nil
P.Y.2011-12 [1.4.2011 to 31.3.2012]	-	Nil
P.Y.2010-11 [1.4.2010 to 31.3.2011]		Nil
	Total	16 days

   The total stay of Ms. Rosy during the previous year in India was less than 182 days and during the four years preceding this year was for 16 days. Therefore, due to non-fulfilment of either of the two conditions for a resident, she would be treated as non-resident for the Assessment Year 2015-16.

   In case of a non-resident, all income accruing or arising in India or deemed to accrue or arise in India or received or deemed to be received in India during the previous year would be taxable.

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Computation of total income of Miss Rosy for the A.Y. 2015-16

Particulars		₹	₹
Income from house property			
Shop in Pune remained on rent from 01.06.2014 to 31.03.2015 @ ₹ 50,000 p.m.			
Gross Annual Value [₹ 50,000 x 10] **(See Note 1 below)**		5,00,000	
Less: Municipal taxes		Nil	
Net Annual Value (NAV)		5,00,000	
Less: Deduction under section 24	₹		
(a) 30% of NAV	1,50,000		
(b) Interest on loan	1,25,000	2,75,000	2,25,000
Income from other sources			
Gifts received from non-relatives is chargeable to tax as per section 56(2)(vii), if the aggregate value of such gifts exceed ₹ 50,000.			
- ₹ 51,000 received from parents of husband would be exempt, since parents of husband fall within the definition of "relative" and gifts from a relative are not chargeable to tax.		Nil	
- ₹ 21,000 received from married sister of husband is exempt, since sister-in-law falls within the definition of "relative" and gifts from a relative are not chargeable to tax.		Nil	
- Gift received from two friends of husband ₹ 75,000 and ₹ 50,000 aggregating to ₹ 1,25,000 is taxable under section 56(2)(vii) since the aggregate of ₹ 1,25,000 exceeds ₹ 50,000 **(See Note 2 below).**		1,25,000	1,25,000
Total income			3,50,000

Computation of tax payable by Miss Rosy for the A.Y. 2015-16

Particulars	₹
Tax on total income of ₹ 3,50,000	10,000
Add: Education cess@2%	200
*Add :*Secondary and higher education cess @1%	100
Total tax payable	10,300

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Notes:

(1) Actual rent received has been taken as the gross annual value in the absence of other information (i.e., municipal value, fair rental value and standard rent) in the question.

(2) If the aggregate value of sum of money received without consideration from non-relatives exceeds ₹ 50,000 during the year, the entire amount received (i.e., the aggregate value of sum of money received) is taxable. Therefore, the entire amount of ₹ 1,25,000 would be taxable under section 56(2)(vii).

(3) Since Miss Rosy is a non-resident for the A.Y.2015-16, rebate under section 87A would not be available to her, even though her total income is less than ₹ 5 lakhs.

2. (i) False: Section 10(2) exempts any sum received by an individual as a member of a HUF, where such sum has been paid out of the income of the family. Therefore, ₹ 50,000 should not be included in Mr. Arun's total income.

(ii) False: Section 11(6) provides that the income for the purpose of application shall be determined without any deduction or allowance by way of depreciation or otherwise in respect of any asset, the cost of acquisition of which has been claimed as application of income under section 11 in the same or any other previous year.

Therefore, the public charitable trust cannot claim depreciation in respect of the laptops for determining the income for the purpose of application, since the cost of laptops has been claimed as application of income in the P.Y.2013-14.

(iii) False: Section 11(7) provides that where a trust has been granted registration under section 12AA and the registration is in force for a previous year, then, such trust cannot claim any exemption under any provision of section 10 [other than exemption under section 10(1) and section 10(23C)].

Therefore, Ramji Charitable trust cannot claim exemption under section 10(35) in respect of income from mutual funds and exemption under section 10(34) in respect of dividends, since it has voluntarily opted for the special dispensation under sections 11 to 13, and consequently has to be governed by the provisions of these sections. However, it can claim exemption under section 10(1) in respect of agricultural income, since section 11(7) provides an exception in respect of such income.

(iv) True: Agricultural income from a land situated in any foreign country is taxable in the case of a person resident in India. Exemption under section 10(1) is not available in respect of such income.

(v) False: Pension received by an individual who has been in the service of the Central Government or State Government and has been awarded 'Maha Vir Chakra' is exempt under section 10(18).

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3. (a) Computation of taxable salary of Mr. Vansh for A.Y. 2015-16

Particulars	₹
Basic pay [(₹ 27,000×11) + (₹ 30,200×1)] = ₹ 2,97,000 + ₹ 30,200	3,27,200
Dearness allowance [30% of basic pay]	98,160
Bonus [₹ 30,200 × 1.5]	45,300
Employer's contribution to Recognized Provident Fund in excess of 12% (18% - 12% = 6% of ₹ 4,25,360)	25,522
Taxable allowances	
Telephone allowance	14,400
Taxable perquisites	
Rent-free accommodation **(See Note 1 below)**	72,759
Medical reimbursement (₹43,000 – ₹15,000) **(See Note 2 below)**	28,000
Reimbursement of salary of housekeeper [₹5,600 × 12]	67,200
Gift voucher **(See Note 3 below)**	Nil
Reimbursement of medical insurance premium **(See Note 4 below)**	Nil
Motor car owned and driven by employee, running and maintenance charges borne by the employer [₹ 48,200 - ₹ 21,600 (i.e., ₹ 1,800 × 12)]	26,600
Value of free lunch facility **(See Note 5 below)**	Nil
Use of laptop and computer **(See Note 6 below)**	Nil
Professional tax paid by employer	2,000
Gross Salary	7,07,141
Less: Deduction under section 16(iii)	
- Professional tax **(See Note 7 below)**	3,000
Salary income chargeable to tax	7,04,141

Notes:

(1) Where the accommodation is taken on lease or rent by the employer, the value of rent-free accommodation provided to employee would be the actual amount of lease rental paid or payable by the employer or 15% of salary, whichever is lower.

For the purposes of valuation of rent free house, salary includes:

(i)	Basic salary	₹ 3,27,200
(ii)	Dearness allowance	₹ 98,160
(iii)	Bonus	₹ 45,300
(iv)	Telephone allowance	₹ 14,400
	Total	₹4,85,060

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15% of salary = ₹ 4,85,060 × 15/100 = ₹ 72,759

Value of rent-free house will be the lower of:

Actual amount of lease rental paid by employer [i.e., ₹ 2,16,000 (₹ 18,000 x 12)]; or

15% of salary (i.e., ₹ 72,759, being 15% of ₹ 4,85,060),

Therefore, the perquisite value is ₹ 72,759.

(2) Any sum paid by the employer in respect of any expenditure actually incurred by the employee on his medical treatment or treatment of any member of his family is exempt to the extent of ₹15,000. Therefore, in this case, the balance of ₹ 28,000 (i.e., ₹ 43,000 – ₹ 15,000) is a taxable perquisite.

(3) If the value of any gift or voucher or token in lieu of gift received by the employee or by member of his household is less than ₹ 5,000 in aggregate during the previous year, the perquisite value is Nil. In this case, the gift voucher was received on the occasion of marriage anniversary and the sum is less than ₹ 5,000. Therefore, the perquisite value of gift voucher is Nil.

(4) Medical insurance premium paid by the employer to effect an insurance on the health of the employee is fully exempt.

(5) Free lunch provided by the employer during office hours is not a perquisite, assuming that the value does not exceed ₹ 50 per meal.

(6) As per Rule 3(7)(vii), facility for use of laptop and computers is an exempt perquisite, whether used for official or personal purpose or both.

(7) As per section 17(2)(iv), a "perquisite" includes any sum paid by the employer in respect of any obligation which, but for such payment, would have been payable by the assessee. Therefore, professional tax of ₹ 2,000 paid by the employer is taxable as a perquisite in the hands of Mr. Vansh. As per section 16(iii), a deduction from the salary is provided on account of tax on employment i.e., professional tax paid during the year.

Therefore, in the present case, the professional tax paid by the employer on behalf of the employee ₹ 2,000 is first included in salary and deduction of the entire professional tax of ₹ 3,000 is allowed from salary.

(b) Computation of gross salary of Mr. Satvik for A.Y. 2015-16

Particulars	₹
Basic salary [(₹12,000 × 10) + (₹13,200 × 2)]	1,46,400
Dearness Allowance (100% of basic salary)	1,46,400
House Rent Allowance (See Note below)	24,560
Gross Salary	3,17,360

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Note: Computation of Taxable House Rent Allowance (HRA)

Particulars	April-May (₹)	June-Oct (₹)	Nov-Dec (₹)	Jan (₹)	Feb-March (₹)
Basic salary per month	12,000	12,000	12,000	12,000	13,200
Dearness allowance (included in salary as per terms of employment) (50% of basic salary)	6,000	6,000	6,000	6,000	6,600
Salary per month for the purpose of computation of house rent allowance	18,000	18,000	18,000	18,000	19,800
Relevant period (in months)	2	5	2	1	2
Salary for the relevant period (Salary per month × relevant period)	36,000	90,000	36,000	18,000	39,600
Rent paid for the relevant period	Nil	32,500 (6,500×5)	17,000 (8,500×2)	8,500 (8,500×1)	17,000 (8,500×2)
House rent allowance (HRA) received during the relevant period (A)	13,200 (6,600×2)	33,000 (6,600×5)	13,200 (6,600×2)	7,200 (7,200×1)	14,400 (7,200×2)
Least of the following is exempt [u/s 10(13A)]					
1. Actual HRA received	13,200	33,000	13,200	7,200	14,400
2. Rent paid – 10% of salary	N.A.	23,500	13,400	6,700	13,040
3. 40% of salary	14,400	36,000 (40% × ₹ 90,000)	14,400 (40% × ₹ 36,000)	7,200 (40% × ₹ 18,000)	15,840 (40% × ₹ 39,600)
Exempt HRA (B)	Nil	23,500	13,200	6,700	13,040
Taxable HRA (Actual HRA – Exempt HRA) (A-B)	13,200	9,500	Nil	500	1,360

Taxable HRA (total) = ₹ 13,200 + ₹ 9,500 + Nil + ₹ 500 + ₹ 1,360 = ₹ 24,560

4. There are two units of the house. Unit I with 2/3rd area is used by Ronak for self-occupation throughout the year and no benefit is derived from that unit, hence it will be treated as self-occupied and its annual value will be Nil. Unit 2 with 1/3rd area is let-out throughout the previous year and its annual value has to be determined as per section 23(1).

Computation of income from house property of Mr. Ronak for A.Y.2015-16

Particulars	Amount in ₹	
Unit I (2/3rd area – self-occupied)		
Annual Value		Nil
Less: Deduction under section 24(b) ₹ 2,60,000 (2/3rd of ₹ 3,90,000) Restricted to		2,00,000
Income from Unit I (self-occupied)		(2,00,000)
Unit II (1/3rd area – let out)		
Computation of GAV		
Step I – Compute Expected Rent (ER)		
ER = Higher of Municipal Value (MV) and Fair Rent (FR), restricted to Standard Rent (SR). However, in this case, SR of ₹ 1,20,000 (1/3rd of ₹ 3,60,000) is more than the higher of MV of ₹ 1,10,000 (1/3rd of ₹ 3,30,000) and FR of ₹ 1,00,000 (1/3rd of ₹ 3,00,000). Hence the higher of MV and FR is the ER. In this case, it is the MV.	1,10,000	
Step 2 – Compute actual rent received/ receivable ₹ 9,200×12 = ₹ 1,10,400	1,10,400	
Step 3 – GAV is the higher of ER and actual rent received/receivable i.e., higher of ₹ 1,10,000 and ₹ 1,10,400	1,10,400	
Gross Annual Value (GAV)		1,10,400
Less: Municipal taxes paid by the owner during the previous year relating to let-out portion 1/3rd of (10% of ₹ 3,30,000) = ₹ 33,000/3 = ₹ 11,000		11,000
Net Annual Value (NAV)		99,400
Less: Deductions under section 24		
(a) 30% of NAV = 30% of ₹ 99,400	29,820	
(b) Interest paid on borrowed capital (relating to let out portion) 1/3 rd of ₹ 3,90,000	1,30,000	1,59,820
Income from Unit II (let-out)		(60,420)
Loss under the head "Income from house property" = (₹2,00,000) + (₹ 60,420) = (₹ 2,60,420)		

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5. Computation of profits and gains of business or profession for A.Y.2015-16

Particulars	₹ (in lakhs)
Profit from business of setting up of warehouse for storage of edible oil (before providing for depreciation under section 32)	29.00
Less: Depreciation under section 32	
10% of ₹ 28 lakh, being (₹ 40 lakh – ₹ 20 lakh + ₹ 8 lakh)	2.80
Income chargeable under "Profits and gains from business or profession"	26.20

Computation of income/loss from specified business under section 35AD

	Particulars	Food Grains	Sugar	Total
		₹ (in lakhs)		
(A)	Profits from the specified business of setting up a warehousing facility (before providing deduction under section 35AD)	15.00	13.00	28.00
	Less: Deduction under section 35AD			
(B)	Capital expenditure incurred prior to 1.4.2014 (i.e., prior to commencement of business) and capitalized in the books of account as on 1.4.2014 (excluding the expenditure incurred on acquisition of land) = ₹ 30 lakh (₹ 70 lakh – ₹ 40 lakh) and ₹ 20 lakh (₹ 50 lakh – ₹ 30 lakh)	30.00	20.00	50.00
(C)	Capital expenditure incurred during the P.Y.2014-15	15.00	10.00	25.00
(D)	Total capital expenditure (B + C)	45.00	30.00	75.00
(E)	Deduction under section 35AD			
	150% of capital expenditure (food grains)	67.50		
	100% of capital expenditure (sugar)		30.00	
	Total deduction u/s 35AD for A.Y.2015-16	67.50	30.00	97.50
(F)	Loss from the specified business of setting up and operating a warehousing facility (after providing for deduction under section 35AD) to be carried forward as per section 73A (A-E)	(52.50)	(17.00)	(69.50)

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Notes:

(1) Weighted deduction@150% of the capital expenditure is available under section 35AD for A.Y.2015-16 in respect of specified business of setting up and operating a warehousing facility for storage of agricultural produce which commences operation on or after 01.04.2012. Food grains constitute agricultural produce and therefore, the capital expenditure incurred for setting up a warehousing facility for storage of food grains is eligible for weighted deduction@150% under section 35AD.

(2) Deduction of 100% of the capital expenditure is available under section 35AD for A.Y.2015-16 in respect of specified business of setting up and operating a warehousing facility for storage of sugar, where operations are commenced on or after 01.04.2012.

(3) However, since setting up and operating a warehousing facility for storage of edible oils is not a specified business, Mr. Prabhakar is not eligible for deduction under section 35AD in respect of capital expenditure incurred in respect of such business.

(4) Mr. Prabhakar can, however, claim depreciation@10% under section 32 in respect of the capital expenditure incurred on buildings. It is presumed that the buildings were put to use for more than 180 days during the P.Y.2014-15.

(5) Loss from a specified business can be set-off only against profits from another specified business. Therefore, the loss of ₹ 69.50 lakh from the specified businesses of setting up and operating a warehousing facility for storage of food grains and sugar cannot be set-off against the profits of ₹ 26.20 lakh from the business of setting and operating a warehousing facility for storage of edible oils, since the same is not a specified business. Such loss can, however, be carried forward indefinitely for set-off against profits of the same or any other specified business.

6. Computation of Gross Total Income of Mr. Jaiprakash for A.Y. 2015-16

Particulars	₹	₹
Sale consideration as per section 50C (Note 1)		95,25,000
Less: Expenses incurred on transfer being brokerage @ 1% of sale consideration of ₹ 85,50,000		85,500
		94,39,500
Less: Indexed cost of acquisition (Note 2) (₹ 1,80,000 × 1024/463)	3,98,099	
Indexed cost of improvement (₹ 10,50,000 × 1024/497)	21,63,380	25,61,479
		68,78,021
Less: Deduction under section 54EC (Note 3)		50,00,000
Long term capital gains		18,78,021

Income from Other Sources		
- Advance received and forfeited on or after 01.04.2014 (Note 4)		7,00,000
Gross Total Income		25,78,021

Notes:

(1) As per section 50C, where the consideration received or accruing as a result of transfer of a capital asset, being land or building or both, is less than the valuation by the stamp valuation authority, such value adopted or assessed by the stamp valuation authority shall be deemed to be the full value of consideration. Where a reference is made to the Valuation Officer, and the value ascertained by the Valuation Officer exceeds the value adopted by the stamp valuation authority, the value adopted by the stamp valuation authority shall be taken as the full value of consideration.

Sale consideration	₹ 85,50,000
Valuation made by registration authority for stamp duty	₹ 95,25,000
Valuation made by the Valuation Officer on a reference	₹ 98,00,000

Applying the provisions of section 50C in the present case, ₹ 95,25,000, being, the value adopted by the registration authority for stamp duty, shall be taken as the full value of consideration for the purpose of computing capital gains.

(2) Since the house was inherited by Mr. Jaiprakash under the will of his father and his father, the previous owner, had purchased the house before 01.04.81, Mr. Jaiprakash has the option to adopt cost incurred by the previous owner or fair market value as on 01.04.81 as cost of acquisition as per section 55(2)(b)(ii). In this case, it is more beneficial to him to adopt the FMV on 01.04.1981 as the cost of acquisition of the house property.

However, indexation benefit will be given effect from the year in which Mr. Jaiprakash first held the asset i.e., P.Y.2003-04.

As per section 51, the advance money forfeited and retained before 01.04.2014, as a result of failure of the negotiations, would be reduced from the cost of acquisition for determining the indexed cost of acquisition for the purpose of computing capital gains.

Computation of indexed cost of acquisition

Particulars	₹
Cost of acquisition	8,30,000
Less: Advance taken in the previous year 2009-10 and forfeited	6,50,000
Cost for the purpose on indexation	1,80,000

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Alternative view: In the case of *CIT v. Manjula J. Shah 16 Taxmann 42 (Bom.),* the Bombay High Court held that the indexed cost of acquisition in case of gifted asset can be computed with reference to the year in which the previous owner first held the asset.

Applying the rationale of the Bombay High Court ruling in this case, the indexed cost of acquisition of house would be ₹ 18,43,200 and long term capital gain would be ₹ 4,32,920. Gross total income, in such a case, would be ₹ 11,32,920.

(3) Exemption under section 54EC is available if the capital gains arising from transfer of long-term capital assets are invested in long-term specified assets, namely, bonds of National Highways Authority of India and Rural Electrification Corporation Ltd. within 6 months from the date of transfer.

As per second proviso to section 54EC(1), out of capital gains arising from transfer of one or more capital assets in a financial year, the investment eligible for exemption cannot exceed ₹ 50 lakhs, whether such investment is made in the same financial year or in the subsequent financial year or in both the years.

In this case, Mr. Jaiprakahsh has invested ₹ 30 lakhs in RECL bonds in the F.Y. 2014-15 and ₹ 35 lakhs in NHAI bonds in the F.Y. 2015-16, both within six months from the date of transfer. However, he would be eligible for exemption of only ₹ 50 lakhs under section 54EC for investment in such bonds.

(4) Advance of ₹ 7,00,000 taken by Mr. Jaipraksh in June, 2014, which was forfeited due to the transaction not materializing, is taxable under section 56(2)(ix). Hence, such amount would not be reduced to compute the indexed cost of acquisition while computing capital gains on sale of the property in November, 2014.

7. Chargeability of receipts under the head "Income from other sources"

S. No.	Taxable/ Not Taxable	Amount liable to tax (₹)	Reason
(i)	Taxable	2,15,000	The exemption from applicability of section 56(2)(vii) would be available if, *inter alia,* any sum of money is received without consideration from a relative or is received on the occasion of marriage of the individual himself. In this case, since the sum of money is received by Mr. Ranu without consideration from a non-relative on the occasion of marriage of his son, it would be taxable in his hands under section 56(2)(vii), since the same exceeds ₹ 50,000.

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(ii)	Not taxable	Nil	Wrist watch is not included in the definition of "property" as per the *Explanation* to section 56(2)(vii). Hence, the value of the wrist watch worth ₹ 52,000 received without consideration from his friend is not taxable in the hands of Sarthak.
(iii)	Taxable	51,000	Brother of husband's grandfather is not included in the definition of "relative". Hence, the amount of ₹ 51,000 received as cash gift would be taxable in Ms. Runjhun's hands.
(iv)	Taxable	87,500	As per section 145A, interest received by the assessee on enhanced compensation shall be deemed to be the income of the year in which it is received, irrespective of the method of accounting followed by the assessee. Interest of ₹ 1,75,000 on enhanced compensation is chargeable to tax in the year of receipt i.e. P.Y.2014-15 under section 56(2)(viii) after providing deduction of 50% under section 57(iv). Therefore, ₹ 87,500 is chargeable to tax under the head "Income from other sources".

8. (i) **Correct:** The clubbing provisions of section 64(1A) are not applicable in a case where the minor child is suffering from any disability of the nature specified in section 80U. The income of such minor child will not be clubbed in the hands of either of the parents. Consequently, the bank interest of ₹ 85,000 and ₹ 90,000 for making bags has to be included in the total income assessed in the hands of Aarav.

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

Therefore, income of ₹ 38,000 arising to her daughter-in-law is chargeable to tax in the hands of transferor i.e., Mrs. Parvati, in this case, since the property was transferred to Mr. Harsh without consideration, with a condition that ₹ 38,000 should be transferred to her daughter-in-law every year.

9. **Computation of total income of Mr. Aaditya for the A.Y. 2015-16**

Particulars	₹	₹
1. **Income from house property**		
House No.1	84,000	
House No.2	(-) 56,000	28,000

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2.	**Profits and gains of business or profession**		
	Profit from leather business	2,50,000	
	Bad debts recovered taxable under section 41(4)	38,000	
		2,88,000	
	Less: Current year loss of textile business	(-) 60,000	
		2,28,000	
	Less: Brought forward business loss of textile business for A.Y.2011-12 set off against the business income of current year	1,05,000	
	Less: Brought forward business loss of chemical business for A.Y.2013-14 set off against the business income of current year	55,000	68,000
3.	**Capital Gains**		
	Short-term capital gain		65,000
Gross Total Income			1,61,000
Less: Deduction under Chapter VI-A			
	Under section 80C – LIC premium paid		18,000
Total Income			1,43,000

Statement of losses to be carried forward to A.Y. 2016-17

Particulars	₹
Loss from specified business (to be carried forward as per section 73A)	80,000
Long term capital loss (to be carried forward as per section 74)	42,000

Notes:

(1) Share of profit of ₹ 21,050 from a firm is exempt under section 10(2A).

(2) As per section 73A, loss of specified business can be carried forward indefinitely for set-off only against profits of any specified business.

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

10. **Computation of total income and tax payable by Mr. Shivpal for the A.Y. 2015-16**

Particulars	₹	₹
Gross total income including long term capital gain and short term capital gain under section 111A		9,25,600

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Less: Long term capital gain		3,15,000
Less: Short-term capital gain under section 111A		64,500
		5,46,100
Less: Deductions under Chapter VI-A:		
Under section 80C (PPF deposit)	1,50,000	
Under section 80D (The deduction would be restricted to ₹ 20,000, since Mr. Shivpal is a senior citizen)	20,000	
Under section 80G (See Notes 1 & 2 below)	18,305	
Under section 80TTA (See Note 3 below)	10,000	1,98,305
Total income (excluding STCG u/s 111A & LTCG)		3,47,795
Total income (including STCG u/s 111A & LTCG)		7,27,295
Total income (rounded off)		7,27,300
Tax on total income (including STCG u/s 111A & LTCG)		
LTCG ₹ 3,15,000 x 20%		63,000
STCG under section 111A ₹ 64,500 x 15%		9,675
Balance total income ₹ 3,47,800 [₹ 3,47,800 – ₹ 3,00,000] x 10%		4,780
		77,455
Add: Education cess @2% and SHEC @1%		2,324
Total tax liability		79,779
Total tax liability (rounded off)		79,780

Notes:

(1) Computation of deduction under section 80G:

Particulars	₹
Gross total income (excluding STCG u/s 111A & LTCG)	5,46,100
Less : Deduction under section 80C, 80D & 80TTA	1,80,000
Adjusted total income	3,66,100
10% of the above	36,610
Contribution made	68,000
Lower of the two	36,610
Deduction under section 80G – 50% of ₹ 36,610	18,305

(2) Deduction under section 80G is allowed only if amount is paid by any mode other than cash, in case of amount exceeding ₹ 10,000. Therefore, the contribution made

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to public charitable trust is eligible for deduction since it is made by way of an account payee cheque.

(3) Deduction of up to ₹ 10,000 under section 80TTA is allowed, *inter alia,* to an individual assessee, if gross total income includes interest income from deposits in a saving account with bank.

11. Computation of total income of Mr. Yashwant for the A.Y. 2015-16

Particulars	₹
Profits and gains of business or profession *(See Working Note 1 below)*	12,47,700
Income from other sources *(See Working Note 2 below)*	82,200
Gross Total Income	13,29,900
Less: Deduction under section 80C (Investment in NSC)	27,000
Total Income	13,02,900

Working Notes:

(1) Computation of profits and gains of business or profession

Particulars		₹	₹
Net profit as per profit and loss account			13,47,000
Add:	Expenses debited to profit and loss account but not allowable as deduction		
	Salary paid to brother disallowed to the extent considered unreasonable [Section 40A(2)]	5,000	
	Motor car expenses attributable to personal use not allowable (₹ 95,000 × ¼)	23,750	
	Depreciation debited in the books of account	95,000	
	Drawings (not allowable since it is personal in nature) [See Note (iv)]	18,000	
	Investment in NSC [See Note (iv)]	27,000	1,68,750
			15,15,750
Add:	Under statement of closing stock		14,000
			15,29,750
Less:	Under statement of opening stock		10,500
			15,19,250
Less:	Contribution to a University approved and notified under section 35(1)(ii) is eligible for weighted		

	deduction@175%. Since only the actual contribution (100%) has been debited to profit and loss account, the additional 75% has to be deducted.		93,750
			14,25,500
Less:	Incomes credited to profit and loss account but not taxable as business income		
	Income from UTI [Exempt under section 10(35)]	28,000	
	Interest on debentures (taxable under the head "Income from other sources")	34,200	
	Winnings from races (taxable under the head "Income from other sources")	33,600	95,800
			13,29,700
Less:	Depreciation allowable under the Income-tax Rules, 1962		82,000
			12,47,700

Notes:

(i) Advertisement expenses of revenue nature, namely, gift of dry fruits to important customers, is incurred wholly and exclusively for business purposes. Hence, the same is allowable as deduction under section 37.

(ii) Disallowance under section 40A(3) is not attracted in respect of cash payment of ₹ 33,500 to Shiva & Co., a goods transport operator, since, in case of payment made for plying, hiring or leasing goods carriages, an increased limit of ₹ 35,000 is applicable [i.e., payment of upto ₹ 35,000 can be made in cash without attracting disallowance under section 40A(3)]

(iii) In point no. 9 of the question, it has been given that depreciation as per Income-tax Rules, 1962 is ₹ 82,000. It has been assumed that, in the said figure of ₹ 82,000, only the proportional depreciation (i.e., 75% for business purposes) has been included in respect of motor car.

(iv) Since drawings and investment in NSC have been given as debited to profit and loss account, the same have to be added back to arrive at the business income.

(2) Computation of "Income from other sources"

Particulars	₹
Interest on debentures	34,200
Winnings from races (₹ 33,600 x 100/70)	48,000
	82,200

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12. (i) According to section 194C, the definition of "work" does not include the manufacturing or supply of product according to the specification by customer in case the material is purchased from a person other than the customer.

Therefore, there is no liability to deduct tax at source in respect of payment of ₹ 2,20,000 to Mr. Arvind, since the contract is a contract for 'sale'.

(ii) As per section 194-IA, any person, being a transferee, responsible for paying to a resident transferor any sum by way of consideration for transfer of any immovable property (other than rural agricultural land) is required to deduct tax at source@1% of such sum, if the consideration for transfer is ₹ 50 lakhs or more. The deduction of tax at source has to be made at the time of credit of such sum to the account of the transferor or at the time of payment of such sum, whichever is earlier.

Therefore, in this case, Mr. Rajesh, the purchaser, is required to deduct tax at source at 1% of ₹ 68 lakhs, being the consideration for transfer of house property, since the sale consideration of house property exceeds ₹ 50 lakhs. However, no tax is required to be deducted by him from the sale consideration payable for transfer of rural agricultural land, since TDS provisions under section 194-IA are attracted in respect of transfer of any immovable property, other than rural agricultural land.

(iii) Since the annual premium exceeds 20% of sum assured in respect of a policy taken on or before 1.4.2012, the maturity proceeds of ₹ 2,30,000 would not be exempt under section 10(10D) in the hands of Miss Sonia, a resident individual. Therefore, tax is required to be deducted@2% under section 194DA on the maturity proceeds of ₹ 2,30,000 payable to Miss Sonia, at the time of payment.

(iv) As per section 194-I, tax is to be deducted @ 2% on payment of rent for plant and machinery, if the payment exceeds ₹ 1,80,000 during the financial year. Since rent of ₹ 1,75,000 paid by a partnership firm does not exceed ₹ 1,80,000, no tax is deductible at source under section 194-I.

(v) 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 to Mr. Devesh for compulsory acquisition of his urban land does not exceed ₹ 2,00,000.

13. (i) False: As per section 140(cd), the return of income of LLP should be verified by a designated partner.

Any other partner can verify the return of income of LLP only in the following cases:-

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

(b) where there is no designated partner.

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(ii) **True:** As per section 140(a)(ii), return of income can be verified by an individual even if he is absent from India. Hence, an individual can himself verify the return of income from a place outside India. Alternatively, any person holding a valid power of attorney and duly authorised by the individual can also verify the return of income. However, such power of attorney should be attached along with the return of income.

14. Since aerated waters are notified under section 4A of Central Excise Act, 1944, excise duty will be payable on the basis of RSP less abatement.

Particulars	(₹)
MRP marked on the bottles of aerated water	30
Less: Abatement @ 40% of MRP [40% of ₹ 30]	12
Assessable Value for purpose of excise duty	18

When more than one MRP is declared on the package of excisable goods, the maximum of such price will be deemed to be the MRP. Thus, if Spring Fresh declares two MRPs namely, ₹ 30 and ₹ 40 on each bottle of aerated water, then ₹ 40 would be deemed to be the MRP. The assessable value for the purpose of excise duty will be calculated in the following manner:-

Particulars	(₹)
MRP marked on the bottles of aerated water	40
Less: Abatement @ 40% of MRP [40% of ₹ 40]	16
Assessable Value for purpose of excise duty	24

15. Computation of customs duty payable

Particulars	(₹)
Assessable value	10,00,000.00
Add: Basic custom duty @ 10% (Note below)	1,00,000.00
Total	11,00,000.00
Add: CVD @12%	1,32,000.00
Add: Education cess @ 2% and Secondary and Higher Eduction Cess @ 1% (3% of custom duty) = 3% of (₹ 1,00,000 + ₹ 1,32,000)	6,960.00
Total for Special CVD [₹ 11,00,000 + ₹ 1,32,000 + ₹ 6,960]	12,38,960.00
Special CVD @ 4%	49,558.40
Total duty payable (₹ 1,00,000 + ₹ 1,32,000 + ₹ 6,960 + ₹ 49,558.40)	2,88,518.40
Total duty payable (rounded off)	2,88,518

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Note: The rate of duty shall be:-

(i) the rate in force on the date of presentation of bill of entry

or

(ii) the rate in force on the date of entry inwards

whichever is later.

No, the answer will not change if the goods are imported in a vehicle. Prior to 06.08.2014, the relevant date for determination of rate of duty and tariff valuation of imported goods by vehicle was date of presentation of bill of entry.

However, section 15 of the Customs Act, 1962 has been amended by the Finance (No. 2) Act, 2014 w.e.f. 06.08.2014 to provide that the relevant date for determination of rate of duty and tariff valuation for imports through a vehicle would be-

(i) the rate in force on the date of presentation of bill of entry

or

(ii) the rate in force on the date of arrival of vehicle

whichever is later.

16. **Computation of central sales tax payable**

	₹	₹
Sales as per bill (including CST)		16,00,000
Less: Weighment dues (Note-1)	-	
Deposits for returnable container (Note-2)	25,000	
Excise duty (Note-3)	-	
Freight charges (Note-4)	60,000	
Goods returned within 6 months of sale	40,000	1,25,000
Turnover including CST		14,75,000
Central sales tax @ 1% $\left(₹14,75,000 \times \frac{1}{101}\right)$ (Note-5)		14,603.96
CST payable (rounded off)		**14,604.00**

Notes:

1. If the service of weighing is in respect of goods and incidental to their being sold, it forms part of sale price.
2. Deposits for returnable container are not includible in the sales price.

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3. Excise duty is a part of sales price.
4. When freight charges are separately charged by dealer, they should be deducted from the sales price.
5. CST on transactions covered by valid 'C' forms is 2% or the sales-tax rate within the State, whichever is lower. Since, in this case, the State sales-tax rate is lower than 2%, the rate of CST is taken as 1%.

17. Computation of Turnover, Input VAT and Output VAT

Goods	Purchases [A]	Input VAT rate [B]	Input VAT credit [C] = [A] x [B]	Sales (Turnover) [D]	Output VAT rate [E]	Output VAT [F] = [D] x [E]
	₹	%	₹	₹	%	₹
P	1,75,000	-	-	3,50,000	-	-
Q (See Note)	2,00,000	12.5	25,000	2,40,000	12.5	30,000
R	2,00,000	4	8,000	2,50,000	4	10,000
Total	5,75,000		33,000	8,40,000		40,000

Computation of Net VAT payable by Sparsh Enterprises

	(₹)
Opening balance of input VAT credit	3,000
Add: Input VAT credit for December, 2014 [C]	33,000
Total Input VAT credit available	36,000
Less: Output VAT payable on taxable turnover [F]	40,000
Net VAT payable	4,000

Note:

	(₹)
Purchase value of goods Q (including VAT)	2,25,000
Less: VAT included in above $2,25,000 \times \frac{12.5}{112.5}$	25,000
Purchase price excluding VAT	2,00,000

18. (a) The compensation for termination of employment will not attract service tax as it is under the terms of employment. Such amount paid by the employer to the employee for premature termination of contract of employment is treatable as amounts paid in relation to services provided by the employee to the employer in

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the course of employment. Hence, amount so paid would not be chargeable to service tax.

(b) As per section 65B(44) of the Finance Act, 1994, only services provided by an employee to the employer are outside the ambit of services under service tax law; services provided outside the ambit of employment for a consideration would be a taxable service liable to service tax. In the present case, Mr. Deepak Jindal is hired as a legal consultant, and hence Mr. Deepak Jindal is liable to pay service tax.

Further, Mr. Deepak Jindal has to register under service tax law, make quarterly payment of service tax (since he is an individual) and file half yearly returns for the half year ending on 30th September and 31st March.

19. (a) In case of taxable service provided by a director of a company to said company, service recipient is liable to pay service tax under reverse charge mechanism.

Further, rule 7 of Point of Taxation Rules, 2011 provides that in respect of persons liable to pay service tax under reverse charge mechanism, the point of taxation shall be the date on which payment is made subject to the condition that payment is made within a period of three months of the date of invoice.

However, if payment is not made within a period of 3 months of date of invoice, point of taxation will be first day that occurs immediately after expiry of said 3 months.

Since, in the present case, payment is made in April end, which is beyond 3 months of the date of invoice (invoice is issued in December), the point of taxation would be the first day that occurs immediately after expiry of said 3 months.

(b) Point of taxation in case of import of service by "associated enterprises" where the person providing the service is located outside India is-

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

OR

(ii) date of making the payment

whichever is earlier

Here, date of debit in PQR Ltd.'s books of accounts is 07.02.2015 and date of payment to Dubai firm is 25.02.2015. Therefore, point of taxation is 07.02.2015.

20. No, Krishna's contention is not correct as non-payment of service tax is not permissible under service tax law on the plea that value of a taxable service cannot be ascertained.

Rule 3 of Service Tax (Determination of Value) Rules, 2006 provides that where the value of a taxable service is not ascertainable, the same shall be determined by the service provider in the following manner:-

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(a) The value of such taxable service would be equivalent to the gross amount charged by the service provider to provide similar service to any other person subject to fulfillment of the conditions below:

1. Such service is in the ordinary course of trade.
2. The gross amount charged is the sole consideration.

(b) Where the value cannot be determined in accordance with clause (a), the service provider will determine the equivalent money value of such consideration. However, such value should, in no case be less than the cost of provision of such taxable service.

Therefore, Krishna should also value the service provided by him in the manner provided by rule 3 of Service Tax (Determination of Value) Rules, 2006 and pay service tax. Accordingly, he should value the service provided by him on the basis of similar services and if that is not possible, he should value the service on the basis of equivalent money value of consideration and pay service tax on the same.

21. With effect from 01.03.2015, aggregators have also been brought within the service tax net by amending the Service Tax Rules, 1994. Aggregator means a person, who owns and manages a web based software application, and by means of the application and a communication device, enables a potential customer to connect with persons providing service of a particular kind under the brand name or trade name of the aggregator. In relation to service provided by a person involving an aggregator in any manner, the aggregator of the service is the person liable for paying service tax.

Since in the given case, Speed Technologies Ltd. fulfills all the conditions of being an aggregator, it will be liable to pay service tax under reverse charge.

However, where the aggregator neither has a physical presence nor does it have a representative for any purpose in the taxable territory, it will have to appoint a person in the taxable territory for the purpose of paying service tax and such person will be the person liable for paying service tax. Therefore, Speed Technologies Ltd. will have to appoint a person in India for the purpose of paying service tax if Speed Technologies Ltd. is located in New York and does not have a representative in India.

22. (i) With effect from 01.04.2015, abatement for classes other than economy has been reduced from 60% to 40%. Therefore, service tax will be payable on 60% of the value of airfare charges in such higher classes. Hence, in the given case, service tax will be payable on 60% of the value of airfare charges paid by Armaan on 15.04.2015 in the following manner:

Service tax = (₹ 1,00,000 × 60%) × 12.36%

= ₹ 7,416.

(ii) No, Raghav's view is not correct. With effect from 01.04.2015, exemption with respect to the services provided by a mutual fund agent to an asset management

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company has been withdrawn. Consequently, services provided by Raghav to ABC Asset Management Company Ltd. are liable to service tax.

Further, in relation to service provided by a mutual fund agent to an asset management company, the recipient of the service would be the person liable for paying service tax. Therefore, in the given case, ABC Asset Management Company Ltd. is liable to pay service tax on the services provided to it by Raghav.

23. Computation of the amount of late fee payable by Fitness Ltd.

Case	Particulars	Late fee as per rule 7C of Service Tax Rules, 1994
Due date for filing return – 25.10.2014		
I.	If period of delay is 15 days from the date prescribed for submission of the return	₹ 500
	In the present case, return has been filed with a delay of 15 (6+9) days from the date prescribed for submission of the return	₹500
II.	If period of delay is beyond 15 days but not later than 30 days from the date prescribed for submission of the return.	₹ 1,000
	In the present case, return has been filed with a delay of 29 (i.e. 6+23) days from the date prescribed for submission of the return	₹ 1,000
III.	Beyond 30 days from the date prescribed for submission of the return	An amount of ₹ 1,000 plus ₹ 100 for every day from the 31st day till the date of furnishing the said return However, total late fee for delayed submission of return shall not exceed ₹ 20,000.
	In the present case, return has been filed with a delay of 92 (i.e. 6+30+31+25) days from the date prescribed for submission of the return	Lower of the following two amounts: (i) ₹ 1,000+ ₹ 6,200 (₹ 100 × 62 days) = ₹ 7,200 (ii) ₹ 20,000 Thus, late fee leviable is ₹ 7,200

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24. (i) Motor vehicle designed to carry passengers is eligible capital goods when used for providing output service of transportation of passengers provided such motor vehicle is registered in the name of service provider. Since in the given case, cars purchased by Safe Cabs Limited are not registered in the name of service provider viz., Safe Cabs Limited, such cars are not eligible as capital goods.

    (ii) Special purpose motor vehicles falling under the heading 8705 are eligible as capital goods for CENVAT credit. Therefore, as per the definition of capital goods, motor vehicles, other than those falling under tariff headings 8702, 8703, 8704 and 8711 used in the factory of manufacturer of final products are eligible as capital goods.

25. (i) With effect from 01.03.2015, time limit for availment of CENVAT credit on inputs has been enhanced from six months to one year of the date of the issue of invoice/bill/challan etc. Thus, in case of the invoice dated 05.03.2015, Mr. Q can take CENVAT credit on inputs after six months of the date of invoice but only upto one year of the date of such invoice. Therefore, the advice of Mr. Q's consultant is not correct.

    (ii) With effect from 01.03.2015, time limit for receiving back the capital goods from job worker to premises of the output service provider has been enhanced from 6 months to 2 years for the purpose of availing CENVAT credit. Thus, the time limit for return of capital goods sent to a job worker on 22.03.2015 for the purpose of availing CENVAT credit is not 180 days, but two years. Therefore, information of Mr. P's consultant is not correct.

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Paper 4: Taxation

Applicability of the Finance Act, Assessment Year etc. for November, 2015 examination

The provisions of income-tax and indirect tax laws, as amended by the Finance (No.2) Act, 2014, including circulars and notifications issued upto 30th April, 2015, are applicable for November, 2015 examination. The relevant assessment year for income-tax is A.Y. 2015-16.

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