PRIME ACADEMY

27th SESSION PROGRESS TEST

FINAL – COST MANAGEMENT

TIME : 2 HOURS **TOTAL : 75 MARKS**

PART A (25 Marks)

(1) The investment for a project is Rs. 20 cr. The selling price per unit shall be Rs 400 with a variable cost of Rs.240 and fixed cost of Rs. 23, 00,000 per annum. If the required rate of return is 12%, what will be the BEP for a life span of 6 yrs?.

(a) 3,18,408 units (b) 3,00,000 units (c) 3,50,408 units (d) 2,18,400 units **(3 Marks)**

(2) If the project building period is 2 years with 60% of capital invested in the 1st year, what is the project BEP production & sale volume?

(a) 3,99,800 units (b) 3,40,299 units (c) 5,00,000 units (d) 3,40,500 units **(1 Mark)**

(3) ABC Ltd. expects to maintain the same inventories at the end of the year as at the beginning of the year. The estimated fixed costs for the year are Rs. 2,88,000, and the estimated variable costs per unit are Rs. 14. It is expected that 60,000 units will be sold at a price of Rs. 20 per unit. Maximum sales within the relevant range are 70,000 units. What is the margin of safety?

(a) 40% (b) 25% (c) 20% (d) 18% **(2 Marks)**

(4) X Ltd provides you the following data to find out the correct value of fixed cost Machine Hours 4,000 and 2,400, Maintenance Cost Rs 6,000 and 5,200 respectively

(a) Rs 5,000 (b) Rs 2,500 (c) Rs 4,500 (d) Rs 4,000 **(1 Mark)**

(5) A firm produces 500 units. The selling price is Rs 4/- and variable cost Rs 2/- per unit. Fixed Cost amount to Rs 800. Find the profit.

(a) Rs 555 (b) Rs 200 (c) Rs 250 (d) Rs 185 **(1 Mark)**

(6) Find the P/V Ratio

	Sales	Profit
First period	Rs 14,433	Rs 385
Second period	Rs 18,203	Rs 1,139

(a) 20% (b) 25% (c) Rs 12% (d) 19.5% **(1 Mark)**

(7) A Ltd has no profit, and then contribution is equal to

(a) Fixed Cost (b) Net Loss (c) Less than Fixed cost (d) Marginal cost **(1 Mark)**

(8) What is the marginal cost equation?

(a) SxU – VxU = F + P (b) F = P (c) SxU = VxU (d) F +P = S **(1 Mark)**

(9) For submission of Tenders the following approach is useful

(a) Incremental Cost (b) Variable Cost (c) Sunk Cost (d) Semi Variable cost **(1 Mark)**

(10) The total cost of a manufactured component is as under:
Prime cost Rs 15, Variable cost Rs 7 and Fixed Cost Rs 4 per unit. The same part is available in the market at Rs 23. Should the firm make it or buy it? (surplus capacity is available)

(a) Make it (b) but it (c) partly makes (d) partly buy **(2 Marks)**

(11) The shut down point can be calculated

(a) (total fixed cost – shut down cost) / Contribution per unit
(b) total fixed cost / contribution per unit
(c) (total fixed cost + variable cost) / Contribution per unit
(d) (total fixed cost + shut down cost) / Contribution per unit **(1 Mark)**

(12) At the point of Economic Order Quantity

(a) Ordering cost = Carrying cost
(b) Ordering Cost > Carrying cost
(c) Ordering Cost + Carrying cost
(d) Ordering Cost < Carrying cost **(1 Mark)**

(13) The assignment problem is another special case of

(a) Linear Programme (b) Simulation (c) Net work Analysis (d) Game theory **(1 Mark)**

(14) A profit- volume graph visually portrays the relationship between

(a) profit and sales (b) Fixed and variable cost (c) profit and loss (d) cost and profit **(1 Mark)**

(15) Which cost is uncontrollable for decision making?

(a) Variable cost (b) incremental cost (c) allocated Fixed cost (d) sunk cost **(1 Mark)**

(16) The superiority of Vogel's Approximation Method (VAM) lies with

(a) Quality of product (b) Unit Cost (c) quantity of product (d) quality and quantity **(1 Mark)**

State whether the following statements are true or false; **(5 x 1 = 5 Marks)**

(17) The essence of management process is decision making

(18) Decision making is one man's job

(19) While making decision, only relevant cost are considered

(20) Past costs are relevant to the decision at hand

(21) Book value of an old equipment is not relevant to the proposal of equipment replacement.

PART - B (50 Marks)

1. Perkins Company has idle capacity. Recently, Perkins received an offer to sell 2,000 units of one of its products to a new customer in a geographic region not normally serviced. The offering price is Rs 10 per unit. The product normally sells for Rs 14. The activity based accounting system provides the following information:

	Cost Driver	Unsed Capacity	Quantity Demanded*	Activity Rate** Fixed	Variable
Direct Materials	Units	0	2,000	--	Rs 3.00
Direct Labour	Direct labor Hours	0	400	--	Rs 7.00
Setups	Setup hours	0	25	Rs 50.00	Rs 8.00
Machining	Machine hours	6,000	4,000	Rs 4.00	Rs 1.00

* This represents only the amount of resources demanded by the special order being considered.

** Fixed activity rate is the price that must be paid per unit of activity capacity. The variable activity rate is the price per unit of resources acquired as need.

Although the fixed activity rate for setups is Rs 50 per hour, any expansion of this resource must be acquired in blocks. The unit of purchase for setups is 100 hours of setup servicing. Thus, any expansion of setup activity must be done 100 hours at a time. The price per hour is the fixed activity rate.

Required:

(a) Compute the change in income for Rerkins Company if the order is accepted. Comment on whether or not the order should be accepted. (In particular, discuss the strategic issues).

(b) Suppose that the setup activity had 50 hours of unused capacity. How does this affect the analysis?

(12 Marks)

2a. Distinguish between Marginal Costing and Absorption Costing

2b. State the limitations of break even chart **(2 x 7 =14 Marks)**

3. A company has four factories situated in four different locations in the country and four sales agencies located in four other locations in the country. The cost of production (Rs. per unit), the sale price (Rs. per unit), shipping cost (Rs. per unit) in the cells of matrix, monthly capacities and monthly requirements are given below:

Factory	Sales Agency 1	2	3	4	Monthly Capacity (Units)	Cost of Production Rs.
A	7	5	6	4	10	10
B	3	5	4	2	15	15
C	4	6	4	5	20	16
D	8	7	6	5	15	15
Monthly Requirements (Units)	8	12	18	22		
Sales Price Rs.	20	22	25	18		

Find the monthly production and distribution schedule which will maximize profit.

(12 Marks)

4. A budgeted profit statement of a company working at 75% capacity is provided to you below,

		Rs.	Rs.
Sales	9,000 units at Rs. 32		2,88,000
Less:	Direct materials	54,000	
	Direct wages	72,000	
	Production overhead:		
	- fixed	42,000	
	- variable	18,000	
			1,86,000
	Gross profit		1,02,000
Less:	Administration, selling and distribution costs:		
	- fixed	36,000	
	- varying with sales volume	27,000	
			63,000
	Net profit		39,000

You are required to:

(a) Calculate the breakeven point in units and in value.

(b) It has been estimated that:

(i) If the selling price per unit were reduced to Rs. 28, the increased demand would utilise 90% of the company's capacity without any additional advertising expenditure, and

(ii) To attract sufficient demand to utilise full capacity would require a 15% reduction in the current selling price and a Rs. 5,000 special advertising campaign.

You are required to present a statement showing the effect of the two alternatives compared with the original budget and to advise management which of the three possible plans ought to be adopted, i.e., the original budget plan or (i) above or (ii) above.

(12 Marks)

PRIME ACADEMY

27^{th} SESSION PROGRESS TEST

FINAL – COST MANAGEMENT

SUGGESTED ANSWERS

PART - A

1	**(a) 3,18,408 units**
2	**(b) 3,40,299 units**
3	**(c) 20%**
4	**(d) Rs 4,000**
5	**(b) Rs 200**
6	**(a) 20%**
7	**(a) Fixed Cost**
8	**(a) SxU – VxU = F + P**
9	**(a) Incremental Cost**
10	**(a) Make it**
11	**(a) (Total fixed cost – shut down cost) / Contribution per unit**
12	**(a) Ordering cost = Carrying cost**
13	**(a) Linear Programme**
14	**(a) profit and sales**
15	**(c) allocated Fixed cost**
16	**(b) Unit Cost**
17	**True**
18	**False**
19	**True**
20	**False**
21	**True**

PART – B

1

(a) The relevant costs are those that change if the order is accepted. These costs would consist of the variable activity costs (flexible resources) plus any cost of acquiring additional activity capacity (committed resources). The income will change by the following amount:

Revnue (Rs 10 x 2,000 units)	= Rs 20,000
Less Increase in resource spending	
Direct Material (Rs 3 x 2,000)	= Rs (6,000)
Direct Labour (Rs 7 x 400 direct labour hours)	= Rs (2,800)
Setup (Rs 50 x 100 hours) + (Rs 8 x 25 hours)	= Rs (5,200)
Machining (Re 1 x 4,000 machine hours)	= Rs (4,000)

Income charge	= Rs 2,000
	==========

Special orders should be examined carefully before acceptance. This order offers an increase in income of Rs 2,000, but it does require expansion of the setup activity capacity. If this expansion is short run in nature, then it may be worth it. If it entails a long term commitment, then the company would be exchanging a one year benefit of Rs 2,000 for an annual commitment of Rs 5,000. In this case, the order should be rejected. Even if the commitment is short term, other strategic factors need to be considered. Will this order affect any regular sales? Is the company looking for a permanent solution to its idle capacity, or are special orders becoming a habit? Will acceptance adversely affect the company's normal distribution channel? Acceptance of the order should be consistent with the company's strategic position.

(b) If 50 hours of excess setup capacity exist, then the setup activity can absorb the special order's activity demands with no additional resource spending required for additional capacity. Thus, the profitability of the special order would be increased by Rs 50,000. thus total income would increase by Rs 7,000 if the order is accepted.

2(a)

Marginal costing	Absorption costing
(i) Only variable costs are considered for product Costing and inventory valuation	Both fixed and variable costs are considered for product Costing and inventory valuation
(ii) Fixed costs are regarded as a period cost	Fixed cost are charged to the Cost of production.
(iii) cost data presented highlight the total contribution And contribution of each product	cost data are presented on conventional pattern.
(iv) The difference in the magnitude of opening stock And closing stock does not affect the unit cost	the difference in the magnitude of opening cost and closing Stock affects the unit cost.

2 (b)

(i) The variable cost line need not necessarily be a straight line because of the possibility of operation of law of increasing returns or law of decreasing returns.

(ii) Similarly the selling price will not be a constant factor.

(iii) When a number of products are produced, separate break even charts will have to be calculated. This poses a problem of apportionment of fixed expenses to each product.

(iv) Break even charts ignore the capital employed in business which is one of the important guiding factor in the determination of profitability.

3

Profit = Sales Price ̃ (Cost of Production + Shipping Cost)

The objective of the company is to maximise the profit. For achieving this objective, let us convert this maximisation problem into minimisation problem by subtracting all the elements of the above pay off matrix from the highest payoff i.e. Rs. 9.

Loss Matrix

Factory	Sales Agency 1	2	3	4	Monthly Capacity (units)
A	6	2	0	5	10
B	7	7	3	8	15
C	9	9	4	12	20
D	12	9	5	11	15
Monthly Requirements	8	12	18	22	

Now, let us apply Vogel's Approximation Method to the above matrix for finding the initial feasible solution

Factory	Sales Agency 1	2	3	4	Monthly Capacity	Difference
A	10 6	2	0	5	10/ 0	2 3 – –
B	7	7	3	15 8	15/ 0	4 0 0 –
C	2 9	9	18 4	12	20 /2/ 0	5 0 0 0
D	6 12	2 9	5	7 11	15 /13/ 6/ 0	4 2 2 2
Monthly Requirement	8 /6 /0	12/ 2/ 0	18 /0	22/ 7		
Difference	1 1 2 3	5 5 2 0	3̃ - - - ̃	3 3 3 1		

Students are requested to find the initial feasible solution by applying the optimality test

Let us introduce ui , vj ,i = (1,2,3,4); j = (1,2,3,4) such that □ij = cij̃ (ui+vj) for allocated cells

Since some of the values of del ij’s are negative, therefore, the above solution is not optimal.
It is recommended to find del ij’s till we are getting non negative values

Factory	**Sales Agency**	**Profit**
A	2	10 x Rs 7 = Rs. 70
B	4	15 x Rs 1 = Rs. 15
C	1	8 x Rs 0 = Rs. 0
C	3	12 x Rs 5 = Rs. 60
D	2	2 x Rs 0 = Rs. 0
D	3	6 x Rs 4 = Rs. 24
D	4	7 x Rs (-2) = Rs.-14
		Total = Rs. 155

4(a)

Contribution and Profitability Analysis

		Total Rs,	**Per unit Rs.**
Sales*		2,88,000	32
Less Variable costs			
Direct material		54,000	6
Direct wages		72,000	8
Production Overheads		18,000	2
Admn , S & D OH		27,000	3
		1,71,000	19
Contribution		1,17,000	13
Less Fixed Overheads Production	42,000		
Admn , S & D	36,000		
		78,000	
		39,000	

*Capacity utilisation : 75%

P/V Ratio = (S – V)/S □ 100 = 40.625%
BE Sales = Fixed costs □ P/V Ratio
= 78,000 □ 40.625%
= Rs 1,92,000

or

1,92,000 □ Rs 32 = 6,000 Units

4(b)(I) Production	90% Capacity (10,800Units) Rs.	100% Capacity (12,000Units) Rs.
Selling price per unit	28	27.20
Variable cost per unit	19	19.00
Contribution per unit	9	8.20
P/V Ratio	31.143%	30.147%
Total contribution	97,200	98,400
Less Fixed Overheads	78,000	83,000
	19,200	15,400

The P/V Ratio has gone down to 31.143% in the case of alternative b(i) and to 30.147% in alternative b(ii). Therefore the company should follow the original plan as at (a) above

		Rs.
4 b (ii)	Selling price per unit .	32
	Less: Variable costs	19
	Contribution per unit	13
	Total contribution (12,000 X Rs 13)	1,56,000
	Less: fixed costs	93,000
	Profit	63,000

This proposal may be expected as there is a considerable increase in the profits.

PRIME ACADEMY

27th SESSION PROGRESS TEST

FINAL – MANAGEMENT INFORMATION AND CONTROL SYSTEMS

Time : 2 Hours **PART-A** **(25 x 1 = 25 Marks)**

1. The process of planning new systems or systems to replace/support existing system is called as :

   a. Systems design
   b. Systems analysis
   c. Systems implementation
   d. System testing

2. Which of the following is not a step involved in preliminary investigation

   a. Request clarification
   b. Feasibility study
   c. Approval of the request
   d. Requirement analysis

3. The basis for the programmers to start coding of the new system is :

   a. Systems analysis
   b. Feasibility study report
   c. Detailed design
   d. User acceptance testing report

4. ____ is the process carried out to ensure that the software does not fail and that it runs according to specifications given by the users :

   a. Feasibility study
   b. System testing
   c. System design
   d. Programming

5. ____ is the process carried out after system is implemented to ensure that the system satisfies user requirement:

   a. Post implementation review
   b. System testing
   c. System design
   d. Feasibility study

6. Salaries to data entry personnel is an example of :

   a. Development costs
   b. Operational costs
   c. Intangible costs
   d. Avoidable costs

7. A brief number, title or symbol used to replace a lengthy or ambiguous/unclear description is called as :

    a. Encryption
    b. Decryption
    c. Firewall
    d. Code

8. Range check, existence check, reasonableness check etc. are examples of:

    a. Input validation
    b. Debugging
    c. Output controls
    d. Encryption

9. The deliverable of the design phase is:

    a. Program prototype
    b. Feasibility study document
    c. Systems manual
    d. Test documentation

10. Which of the following is not an feature associated with buying the software off the shelf:

    a. Rapid implementation
    b. Low risk
    c. High costs
    d. Good product quality

11. When companies do not have internal expertise to evaluate a vendor's proposal, the method to be adopted is :

    a. Checklists
    b. Public evaluation reports
    c. Point scoring analysis
    d. Feasibility study

12. Checking the system using the documents/inputs available without actually using it for test is called as

    a. Benchmarking test
    b. Business continuity planning
    c. Desk checking
    d. Test cases

13. Sample problems which reflect at least some portion of the buyer's real work environment data and process is called as :

    a. Benchmark problem
    b. Test cases
    c. Business continuity planning
    d. Desk checking

14. A conversion procedure where on a specified date old system is dropped and new system is put to use is called as:

    a. Direct change over method
    b. Parallel conversion method
    c. Gradual conversion method
    d. Distributed conversion method

15. A conversion which involves full implementation of the system in one branch of the organisation and then replicating it in all other branches is called as:

    a. Direct change over method
    b. Parallel conversion method
    c. Gradual conversion method
    d. Distributed conversion method

16. An organization wanting to know if the system's hardware, software and personnel are capable of performing their duties and whether they are actually performing them should carry out an:

    a. Information evaluation
    b. Development evaluation
    c. Schedule feasibility
    d. Operational evaluation

17. A feature of ERPs where modules can be interfaced or detached without affecting the other modules is called as :

    a. Flexibility
    b. Modularity
    c. Comprehensive
    d. Best business practices

18. Which of the following is not a component of BPR ?

    a. Fundamental re-thinking
    b. Testing
    c. Radical redesign
    d. Dramatic improvements

19. Controls for a variety of exposures that cause a threat to computer based information system is called as:
    a. General Controls
    b. Application Controls
    c. Management Controls
    d. Audit Controls

20. One of the control objectives of an operating system which states that applications must not be able to gain control over the Operating System leading it to malfunction or destroy data is referred to as :

    a. Operating system to protect users from one and other
    b. Operating system to protect itself from users
    c. Operating system to protect users from themselves
    d. Operating system to be protected from itself

21. In an operating system, the first line of basic defense against un-authorised access is called as :

    a. Firewalls
    b. Routers
    c. Log-on procedures
    d. Intrusion detection system

22. An access control mechanism wherein the resource owners are given certain privileges and they in turn give powers/rights to other users is called as :

    a. Centralized access control
    b. Random access control
    c. Sequential access control
    d. Discretionary access control

23. Detection of unauthorized access, reconstruction of events and personal accountability are objectives of which of the following control?

    a. Audit trails
    b. Firewalls
    c. Anti-virus software
    d. Data back-up

24. A component of DRP which outlines action to be taken immediately after a disaster occurs is called as :

    a. Recovery Plan
    b. Back-up Plan
    c. Emergency Plan
    d. Test Plan

25. An organization wanting to implement perimeter security to the organisations network from the external network should implement a :

    a. Firewall
    b. Router
    c. Switch
    d. Modem

PART-B

(50 Marks)

Answer any Two Questions

1.(a) Explain the six stages of SDLC in brief (12 Marks)

(b) List the guidelines for design of printed outputs (8 Marks)

(c) Briefly describe the concept of public evaluation reports as a method of validating vendor's proposal (5 Marks)

2 (a) Discuss the meaning, advantages and disadvantages of various conversion strategies (10 Marks)

(b) "Any system should possess a few key characteristics to qualify for a true ERP solution" - Explain (10 Marks)

(c) Explain batch controls as an input control measure (5 Marks)

3. Write Short Notes on the following : (5 x 5 = 25 Marks)

a. Source Program library controls
b. Program version number
c. Disaster recovery planning
d. Operator intervention controls
e. Business process re-engineering

PRIME ACADEMY

27th SESSION PROGRESS TEST

FINAL – MANAGEMENT INFORMATION AND CONTROL SYSTEMS

PART – A

1	a
2	d
3	c
4	b
5	a
6	b
7	d
8	a
9	c
10	c
11	b
12	c
13	a
14	a
15	d
16	d
17	b
18	b
19	a
20	b
21	c
22	d
23	a
24	c
25	a

PART - B

1(a) The Six stages in brief

Stage 1: Preliminary investigation:

- **When undertaken:** Preliminary investigation is undertaken when users come across a problem or an opportunity and submit a formal request for a new system to the MIS department.

- **Steps involved :** Preliminary investigation consists of three broad steps

  1. **Request clarification**: Requests submitted by the users may require some clarification before system investigation can commence. This is to determine as to what the user actually wants.

  2. **Feasibility study:** The system analyst carries out technical, financial, operational, schedule and legal feasibility study to determine whether the proposed system is feasible or not.

  3. **Approval of the request:** Some requests may get eliminated at the feasibility study stage. Based on the analyst's observations, the management decides which system should be taken up for development. Approval is critical as management commits resources (capital, manpower) at this stage.

Stage 2: Requirement Analysis or Systems Analysis:

- Once the management decides to go ahead with the development , the user needs should be studied in detail.

- The systems analyst uses various tools like interviews, questionnaires, environment analysis to understand the requirements.

- He identifies the problems and short comings of the existing system which should be addressed in the new system

Stage 3: Design of the system (Blue Print):

- The user requirements as identified are incorporated in the design of the new system.

- In this stage various reports, outputs, inputs, files are designed to show how user requirements will be met.

- The detailed design is then given to the programmers so that they can start the development(i.e. coding/programming).

(Similar to how the architect's plans are given to the construction contractor to start construction activity)

Stage 4: Development and Acquisition of software:

- After resolving the design details, resources needed like hardware, software are determined.

- The organisation may decide buy or lease or to develop the software in-house

- If the software is to be developed in-house, the analyst works closely with the programmers and also works in the documentation of the software and the procedure manuals.

Stage 5: Systems Testing:

- Before information system can be introduced in live/production environment, it needs to be tested to ensure that software does not fail and that it runs according to specifications given by the users.

- Set of test data (called as test cases) are fed into the new system and the results examined with the expected results. Afterwards the new system may be fed with sample live data and results examined.

  Ex: To test a tax-module we would key in the details and obtain the final tax payable. This would be checked with the calculations done manually to ensure that the system works correctly.

(**Note:** There are various approaches to testing like systems testing, unit testing, interface testing and stress testing)

Stage 6: Implementation and Maintenance:

- After a system passes through the testing process, it is implemented in live area.
- New hardware if required is installed and users are trained to work on the new system.
- After the system has stabilised in live area, it is monitored to ensure that it satisfies user requirements.

It may also undergo some maintenance efforts to adapt to changing user and business needs.

1(b) **Design of printed output**

Meaning: It is the arrangement of items/data variables on the output medium.

Contents

Output layouts are mocks/samples of the actual report that the system will generate when in real operation.

- It should show the location/position of all variables like amounts, total, summary information, pre-printed headings (like company name, logo).

- Items to be included in the report should be factored in from the information collected during the requirement analysis phase.

Some guidelines for design of printed output

i. Reports should read from left to right and top to bottom

ii. The critical items should be clearly visible/identifiable

iii. Report should contain heading/title, page number, date of report preparation (Ex: Tally reports) etc.

Heading/title➔ gives an idea to the user as to what is expected out of the report.

Page numbers ➔ help the user to reference the data

iv. Each data item should have an heading to describe it (for example amount columns in a bill should read " Amount (Rs.)")

v. Related items should be group together to enable better comprehension.

vi. Control breaks ➔ help increase readability ➔ should be boxed or marked with special characters to draw attention to important items.

vii. The detail line used to fill each row/field should contain the instructions of filling up the space. For example in the name field it should read " alphabets in capital letters, initial separated by decimal dot"

The sample/mock reports should be reviewed by users for its usefulness, readability, aesthetic appeal etc.

1(c) Public evaluation reports: Some consultancy agencies compare and contrast performance of various software and hardware and publish these reports. These reports are used by companies wanting to invest in new software/hardware and especially useful when company staff do not have much systems knowledge.

2(a)

Conversion method	***Meaning***	***Advantages***	***Disadvantages***
1. Direct change over method (also called Plunge Method)	On a specified date old system is dropped and new system is put to use Can be adopted only if extensive testing done beforehand	Users straight away use the new system- adaptation easy.	1. Risky 2. Long delays if errors occur since this the only system available to do the processing 3. Users resent/resist since unfamiliar system 4. Cannot compare results with the old system(since old system has been discarded)

Conversion method	Meaning	Advantages	Disadvantages
2. Parallel conversion	Running the old system and the new system in parallel at the same time Results of the new system compared with that of the old system and if reliable over a period of time, old system is stopped and new system put to use.	1. Since data available from both old and new systems, any errors in new system can be corrected. 2. Users feel secure as they are not faced with abrupt change	1. Cost of running both systems (old and new) is very high. 2. Employees work load increases during conversion. 3. Unless new system is replacing old manual system, output comparison difficult. 4. If new system is an improvement over existing system, outputs would differ and hence difficult to compare. 5. Users familiar with old system and will continue to use only that.

Conversion method	Meaning	Advantages	Disadvantages
3. Gradual conversion	Attempts to combine the good features of parallel and direct changeover method. Volume of transaction gradually increased ➔ new system is phased in.	Users can use the new system gradually and there is a possibility of detecting and correcting errors without much system downtime.	1.Time consuming as it may take a long time to put the new system in use. 2. Not the best method for small, simple systems.
4. Modular prototype conversion	Involves building of modular, operational prototypes to change from old to new system. Each module is modified, accepted and put to use gradually.	1. Thorough testing of modules before being put to use. 2. User familiarity before model put to use.	1. Too many prototypes and hence may not be feasible. 2. Interfacing of the various modules (so that they work as a system) may be a problem.
5. Distributed conversion (Also	Involves full implementation of the	Problems if any can be identified	Each branch/site may have its own

called as PILOT run)	system in one branch of the organization (say a bank branch) using any of the above four methods. If successful then carried out at other branches.	and controlled in one location rather than affecting all locations.	problem that needs to be handled separately. Hence success in one site does not necessarily mean success in other sites.

2(b)

S.No.	***Characteristic***	***Meaning***
1	Flexibility	• Should be flexible to meet the changing needs of business • C/S technology enables ERP to run across various database back ends through ODBC
2.	Modular & Open	• ERP should have open system architecture- refers to a system where modules can be interfaced/detached without affecting other modules. • Should support various heterogeneous hardware platforms. • Should support third party add-ons also.
3.	Comprehensive	• Should support variety of organisational functions • Should suit wide range of business
4.	Beyond the company	• Should not be confined to the organisation. Should support on-line connectivity to the other business entities.
5.	Best Business practices	• Should contain the industry best practices • It imposes its own logic on a company's strategy, culture & organisation • **Ex**: ERPs should support implementation of Sarbanes-Oxley Act

2 (c) <u>Batch controls</u>

Meaning: These are effective methods of managing high volumes of data through a system.

Objective:

- To reconcile output produced by the system with the inputs originally entered into the system.
- To ensure that :

1. All records in the batch are processed (completeness in processing).
2. No records are processed more than once (no duplicate processing).
3. Audit trails are created to trace transactions from input thru' to processing and finally to the output.

Methods to achieve the above objectives

- Group similar type of input transactions (**Ex**: All cheques for clearing in a bank are grouped into batches for entry) into batches and then control the batches throughout the data processing stages.
- Two documents used in the process are :

  1. Batch transmittal sheet
  2. Batch control log

3a. Source program library controls:

Meaning of source program library (SPL): It refers to a place where the source computer programs are stored

Two possible situations

Programmers have Unrestricted access To program library	Programmers have controlled access to program library
⇩	⇩
Extremely risky	Ideal situation

Situation 1: Programmer has unrestricted access to SPL

- Extremely risky -worst case scenario.
- If programmers have unrestricted access to SPL,

⇩

Cannot detect unauthorised changes

⇩

It is a control weakness as programs are subject to unauthorised changes

⇩

Other controls become in-effective and program's integrity cannot be verified.

Situation 2: A controlled SPL environment

- To control SPL , there must be protective controls procedures
- Some controls to be place are:

  1. Controls on how programs are stored in SPL
  2. Controls on retrieval of programs for maintenance
  3. Controls over how obsolete programs are deleted / purged in a library
  4. Documentation of program changes to provide an audit trail.

(These controls are very similar to how one can borrow books from a public lending library)

Methods to implement these controls

A **SPL management software** is required which may either be supplied by the vendor or may be in-house developed.

3b. Program version number

- Version number refers to a control number assigned by the SPL management system
- When programs first placed in library for implementation ➔ assigned version number 0 .
- With every modification version number increased by 1.
- This feature along with audit trails provide basis for identification of unauthorised changes that have been effected.
- **Ex:** if the version number of the program is 10 but auditor finds that only 7 changes have been authorised , it can mean two things:

Authorised changes have occurred → but documentation has not been generated	Unauthorised changes have been effected ➔ needs to be probed further

3c. Disaster recovery plan (DRP)

Meaning:

- Refers to contingency measures that the organisation should adopt to recover from or prevent any disaster(disaster could be flood, earthquake etc. or any violent act of terrorism that could ruin the organisation).

Purpose/objective

- To assure the management that in case of any disaster :
  1. Normalcy would be restored within a set time
  2. Hence impact of loss would be minimized.

Components of a DRP

⇩	⇩	⇩	⇩
Emergency plan	Recovery plan	Back-up plan	Test plan

3d. Operator intervention controls

- System may sometimes require operator intervention to initiate some actions like :
  - ❖ Entering control totals for a batch of records
  - ❖ Providing parameter values
  - ❖ Activating program from a different point (other than from start point) while re-entering semi-processed error records.

- Operator intervention increases chances of human errors. Hence systems with limited operator's intervention are less prone to processing error.

Operator intervention cannot be eliminated. However they can be reduced by logical derivation of parameter values, program start points etc.

3e. Business Process re-engineering

- Every company wanting to implement an ERP has to reengineer its processes (activities) in order to suit to the ERP.

- It is a fundamental **rethinking, radical redesign of processes/activities to achieve dramatic improvements in performance like quality and cost saving.**

➢ <u>Fundamental rethinking</u>: refers to asking questions like "why do we do a process – what value does it add?". If a process does not add any value, it may better be dropped rather than simplifying/automating it.

➢ <u>Radical redesign</u>: refers to reinventing processes and not just enhancing or improving. It uses methods like "clean slate approach" (similar to zero based budgeting (ZBB))

➢ <u>Dramatic improvements</u>: Aims to achieve 80% to 90% reduction in costs. It is possible only through major improvements/breakthroughs and not through small incremental changes.

PRIME ACADEMY

27th SESSION PROGRESS TEST

FINAL – DIRECT TAXES

Time: 2 Hours **PART-A** **(25 x 1 = 25 Marks)**

1. The Central Board of Direct Taxes does not have the power to waive interest u/s.
   (a) 234B
   (b) 201(1A)
   (c) 220(2)
   (d) 234A

2. Where the jurisdiction of the Assessing Officer is questioned the issue shall be determined by
   (a) Director General / Chief Commissioner / Commissioner of Income Tax
   (b) Central Board of Direct Taxes
   (c) Additional Commissioner of Income Tax
   (d) Joint Commissioner of Income Tax

3. Where there is a change in the incumbent of an office of an income tax authority
   (a) the successor can proceed without rehearing the assessee
   (b) the successor cannot proceed without rehearing the assessee
   (c) the successor can proceed without hearing the assessee but where demanded has to rehear the assessee

4. A search and seizure operation can be authorized by
   (a) the Central Board of Direct Taxes
   (b) the Assistant Commissioner of Income Tax
   (c) Director General of Income Tax
   (d) the Deputy Director of Income Tax

5. In a search and seizure operation the following cannot be seized
   (a) stock in trade
   (b) books of account
   (c) documents
   (d) money, bullion, jewellery

6. The seized assets can be applied first towards
   (a) liability arising as a result of existing liabilities
   (b) liability arising as a result of search
   (c) at the option of the Assessing Officer
   (d) at the option of the assessee

7. The following are mandatorily required to file a return even if the income does not exceed the maximum amount not chargeable to tax
   (a) individual
   (b) HUF
   (c) Co-operative society
   (d) Partnership Firm

8. The loss that can be carried forward even if the return is not filed within the due date
   (a) Loss under the head income from house property
   (b) Loss under the head capital gains
   (c) Loss under the head profits and gains of business or profession
   (d) Loss under the head income from other sources

9. Self assessment tax is first to be adjusted towards
   (a) Tax and balance towards interest
   (b) Interest and balance towards tax
   (c) At the option of the assessee
   (d) At the option of the Assessing Officer

10. A notice u/s.142(1)(i) requiring the assessee to file a return can be issued only
    (a) within the time allowed to furnish a return u/s.139(1)
    (b) any time after the time allowed to furnish a return u/s.139(1)
    (c) any time after the time allowed to furnish a return u/s.139(1) but before the end of the relevant assessment year
    (d) after the time allowed to furnish a return u/s.139(4)

11. A revised return can be filed
    (a) if the original return is filed within the time allowed u/s.139(1) or in response to a notice u/s.142(1)
    (b) even if the original return is filed u/s.139(4)
    (c) if the original return is filed within the time allowed u/s.139(1) or in response to a notice u/s.142(1) and there is a omission or wrong statement in such return

12. A special audit can be directed
    (a) only when the assessee is subject to audit u/s.44AB
    (b) whether or not the assessee is subject to audit u/s.44AB
    (c) only if the assessee is not subject to audit u/s.44AB

13. A notice u/s.143(2) should be served on the assessee before
    (a) the end of the relevant assessment year
    (b) 12 months from the end of the month in which the return is filed
    (c) 12 months from the end of the financial year in which the return is filed
    (d) 12 months from the date on which the return is filed

14. An opportunity of being heard before passing a best judgment need not be given where
    (a) a notice u/s.143(2) has been issued
    (b) a notice u/s.148 has been issued
    (c) a summon u/s.131 is issued
    (d) a notice u/s.142(1) has been issued

15. Where the reopening is to give effect to a finding or direction in an order of appeal, revision, reference or of any Court, the time limit to initiate reassessment proceedings would be
    (a) four years from the end of the relevant assessment year
    (b) six years from the end of the relevant assessment year
    (c) without any time limit except where the reassessment was already barred by limitation when the order which gave rose to the appeal, reference or revision was the subject matter of appeal, reference or revision
    (d) without any time limit

16. An order of reassessment has to be passed before the expiry of
    (a) 12 months from the end of the financial year in which the notice u/s.148 is issued
    (b) 9 months from the end of the financial year in which the notice u/s.148 is issued
    (c) 12 months from the end of the month in which the notice u/s.148 is issued
    (d) 9 months from the end of the month in which the notice u/s.148 is issued

17. Where an assessment is reopened consequent to a direction of an appellate authority, revisionary authority or Court the approval for reopening must be obtained from
    (a) the Additional Commissioner of Income Tax
    (b) the Commissioner of Income Tax
    (c) the Chief Commissioner of Income Tax
    (d) no approval needs to be obtained

18. Where there is a search or requisition, an assessment under section 153A is to be done with reference to
    (a) six years preceding the year of search or requisition
    (b) only the year of search or requisition
    (c) five years preceding the year of search or requisition and including the year of search or requisition
    (d) none of the above

19. Where there is a search or requisition
    (a) all pending assessments and appeals shall abate
    (b) all pending assessments and revisions shall abate
    (c) all pending assessments shall abate
    (d) all pending appeals shall abate

20. The time limit for completing an assessment u/s.153B where there is a search or requisition will apply
    (a) to the year of search
    (b) to the six years preceding the year of search as well as the year of search
    (c) to the six years preceding the year of search
    (d) none of the above

21. A mistake can be said to be apparent when
    (a) the issue is debatable
    (b) the issue is one which can be decided on the basis of a long drawn process of investigation
    (c) the issue is not debatable
    (d) the issue is not debatable and does not involve a long drawn process of investigation

22. A public charitable trust can utilize the accumulated income

    (a) for all or any of the objects of the trust
    (b) only for the objects stated as the purpose for which it is accumulated
    (c) as contribution to another charitable trust
    (d) all of the above

23. A public charitable trust has to apply for registration with the Commissioner of Income Tax

    (a) within 6 months of creation of the Trust
    (b) within 6 months from the end of the month in which the trust is created
    (c) within 1 year of creation of the Trust
    (d) within 1 year from the end of the month in which the trust is created

24. Interest on capital borrowed for a business will not be allowed as a deduction

    (a) if it is borrowed for working capital
    (b) if it is borrowed to acquire capital assets
    (c) if it is borrowed for acquiring capital assets at the time of extension of the existing business
    (d) if it is borrowed for acquiring capital assets at the time of extension of the existing business until the asset is first put to use

25. For claiming exemption in respect of capital gains by reinvestment in bonds, the reinvestment should be made

    (a) within 3 months from the end of the month in which the transfer took place
    (b) Within 6 months from the date of transfer
    (c) Within 3 months from the end of the financial year in which the transfer took place
    (d) Within 6 months from the end of the financial year in which the transfer took place

PART-B

(50 Marks)

1. The assessee was a shareholder in a company. As the company went into liquidation, assets of the company were distributed to the shareholders. The assessee was distributed agricultural land. The assessee contends that since agricultural land is not a capital asset, capital gains cannot be assessed in her hands. Is the claim of the assessee tenable?

   \- 4 Marks

2. The assessee company has paid excise duty on certain goods in the year 2001. On appeal the first appellate authority as well as the CEGAT held that the goods were not liable to duty. Subsequently the excise duty was refunded on 26.06.2007. The appeal preferred by the excise department was dismissed by the High Court. The excise department filed a special leave petition before the Supreme Court which was still pending. For the assessment year 2008-09 the Assessing Officer wants to tax the same by invoking section 41(1) while the assessee contends that the same cannot be taxed. Express your opinion on the issue.

   \- 4 Marks

3. An assessee sold her house property and out of the sale proceeds acquired 15% share in another house property owned by her husband and son. The assessee was residing in this house prior to the purchase and continued to reside in the same house after purchase. The assessee wants to claim exemption u/s.54 in respect of the investment by way of purchase of part of the house. Will the same be available to the assessee?

   \- 4 Marks

4. The assessee had inherited property on her husband's death. The husband of the assessee had mortgaged the said property which mortgage was vacated by the assessee. The assessee claimed that the amount so paid to clear the mortgage was to be treated as cost of acquisition. Is this a correct view? Would your answer be different if the mortgage was not created by the husband before his death but by the assessee herself?

   \- 4 Marks

5. An assessment was made on an assessee u/s.143(3) without the service of a notice u/s.143(2). The assessee had explicitly given a waiver in writing from the receipt of such notice. The assessee contends that the assessment u/s.143(3) is invalid despite his consent as no notice u/s.143(2) has been served on him. Comment.

   \- 4 Marks

6. Can an assessee claim deduction in the course of reassessment proceedings?

   \- 4 Marks

7. County Ltd was a wholly owned subsidiary of Attorney Ltd. Attorney Ltd had lent money to County Ltd for the purpose of its business. Since County Ltd was in financial difficulty, it was decided by the Board of Directors of Attorney Ltd through a resolution passed in May 2008 that no interest would be charged from County Ltd for the previous year 2007-2008. On the basis of this resolution Attorney Ltd did not account for the interest from County Ltd as income for the assessment year 2008-09. Is this tenable?

- 4 Marks

8. A taxpayer receives discounted interest on investment in Government Bonds for a period of 3 years in the year in which the bond is issued. The assessee is following the cash system of accounting. The assessee is of the view that he could offer 1/3rd of the discounted interest as income for a period of 3 years. Is this correct? Would the answer be different if the assessee is following the mercantile system of accounting?

- 4 Marks

9. The assessee sold a residential house and reinvested in another residential house. However the house had not been registered in the name of the assessee though the consideration had been paid by the assessee and possession had been handed over to the assessee within the time stipulated in section 54 for the purpose of reinvestment. Can the assessee claim the exemption u/s.54 in such a case where the registration is beyond time? Would the view be different if the registration was within time while the payment was beyond the time contemplated for making investment u/s.54?

- 4 Marks

10. Marshall was the owner of a land and building. The land was purchased about 10 years back while the building on the said land was constructed a year ago. The land and building was sold for a value of Rs.80 lakhs in the previous year 2007-08. Marshall is of the view that the entire gain on the sale should be treated as long term capital gains while the Assessing Officer is of the view that the entire gain should be taken as a short term capital gain. Whose view is the correct one?

- 4 Marks

11. Should an assessing officer disclose reasons for initiating reassessment proceedings by the issue of a notice under section 148 at the time of issue of such notice? Can an assessee demand for the reasons after furnishing a return in response to such notice?

- 5 Marks

12. Will loss from dealing in shares by an individual be treated as speculative loss or business loss? What will be your view if the dealing is not of shares but of derivatives? You may assume that the transactions in question are not transactions resulting in capital gains but the activity is carried on as a business.

- 5 Marks

PRIME ACADEMY
27th SESSION PROGRESS TEST
FINAL – DIRECT TAXES
Suggested Answers

PART – A

1. c
2. a
3. c
4. c
5. a
6. b
7. d
8. a
9. b
10. c
11. c
12. b
13. b
14. d
15. c
16. b
17. d
18. a
19. c
20. b
21. d
22. b
23. c
24. d
25. b

PART – B

1. Section 46(1) of the Income Tax Act, 1961, opens with a non obstante clause and provides that despite what has been provided in section 45, the distribution of assets by a company on its liquidation to its shareholders is not to be regarded as a transfer by the company for the purposes of section 45. Section 46(2) of the Act, however, specifically provides that the money or other assets, which a shareholder may receive from a company on its liquidation shall be chargeable to income tax under the head "Capital gains" and thus create a charge on such monies or assets. Section 46(2) of the Act is, therefore, an independent charging section and in construing that provision recourse to the other provisions of the Act, are only required to be made to the extent expressly or impliedly required by that provision itself. Section 46(2), after making the money or assets received by the shareholder chargeable to income tax under the head "Capital gains" provides that the amount to be charged to tax, is the amount received or the market value of the asset as on the date of distribution as reduced by the amounts assessed, as dividend within the meaning of section 2(22)(c) of the Act. It further provides that the amount so calculated shall be deemed to be the full value of consideration for the purpose of section 48. It must be noticed that the words used in the section in relation to assets are not "capital assets", but other assets. The term "asset" has not been defined in section 2. The exclusion of agricultural lands to the extent provided in section 2(14)(iii)(a) is, therefore, only for the purpose of not treating such lands as capital assets. The fact that agricultural lands are not capital assets to the extent provided in the definition does not, however, imply that they are not assets at all. The value of agricultural lands received by the assessee on the liquidation of the company could be charged to tax under section 46(2).

2. The ingredients of section 41(1) were satisfied in the instant case and, therefore, the amount of excise duty refunded became taxable during the year in question. This was a case in which the assessee could be said to have obtained the amount by way of refund in respect of the business expenditure incurred by it during an earlier year, for which assessee had the benefit of deduction or allowance. In the instant case, it was the first clause that squarely applied but not the second one. Whether there was cessation or remission of liability was an irrelevant line of enquiry. The correct way of understanding section 41(1) is to read it with the latter clause 'some benefit in respect of such trading liability by way of remission or cessation thereof' as a distinct and self-contained provision. To read the phrase, 'by way of remission or cessation thereof', as governing the previous clause as well, i.e. 'obtained any amount in respect of such loss or expenditure', would be doing violence to the language and structure of the provision. That apart, the operation of the provision, which is designed to have widest amplitude will get constricted and truncated by reason of such interpretation. In the light of the above discussion, there was no merit in the appeal and the same deserved to be dismissed. *[Polyflex (India) Pvt Ltd v CIT [2002] 257 ITR 343 (SC)]*

3. When the Act enables an assessee to get exemption from payment of tax in respect of purchase or construction of a residential house, purchase or construction of a portion of the house should also enable the assessee to claim the exemption. It is possible that a person may not be in a position to purchase the whole residential house at a time and in the circumstances might purchase a portion of the house or some interest in the house. Further, section 54 nowhere states that a residential house which is purchased by the assessee so as to avail the exemption should not be one in which the assessee was residing. When the section does not put such an embargo, it would be absolutely against the settled principles of interpretation of statute to read such an intention of the legislature so as to deprive an assessee from getting the exemption u/s.54. In such a case, if there is a *bona fide* purchase, the revenue cannot be permitted to say that the assessee is not entitled to exemption u/s.54 merely because the assessee was residing in the house which was purchased by her. *[CIT v Chandanben Maganlal [2002] 120 Taxman 38 (Guj)]*

4. 4. If the property is mortgaged by the previous owner, then the amount paid to discharge the mortgage debts could be treated as cost of acquisition and allowed as a deduction. However if the mortgage is created by the assessee, the amount paid to discharge the same could not be treated as cost of acquisition and allowed as a deduction. *[VSMR.Jagadishchandran v CIT [1997] 227 ITR 240 (SC), Rm.Arunchalam v CIT [1997] 227 ITR 222 (SC)]*

5. The right to receive a notice u/s.143(2) cannot be relinquished or abandoned. The concept of waiver or the right to receive a notice can be applied only where such a notice or the waiver of any act required to be done is not a prerequisite for conferring jurisdiction. This will be the position even where the waiver has explicitly been given in writing by the assessee. A notice u/s.143(2) is one that vests on the Assessing Officer the right to complete an assessment u/s.143(3) since such a notice is one that vests with an assessing officer jurisdiction. Therefore, the requirement for service of such a notice cannot be waived. It has been held in the case of *Karam Chand Thapar & Bros. (Coal Sales) Ltd. v DCIT (1997) 228 ITR 317(Cal)* that mere compliance with an invalid notice will not take away a right subsisting in an assessee to challenge the assessment on the ground of invalidity of the notice. The Court further held that where the validity of a notice has not been questioned at the time of assessment, it can be questioned at the appellate forum and where the non service or the service beyond the time stipulated is proved, the order would be void.

6. The Supreme Court in *Chettinad Corporation Pvt Ltd v CIT (1993) 200 ITR 320 (SC)* has held that an assessee could only be permitted to claim allowances/relief which are relevant to the items which are the subject matter of the enquiry during reassessment. The Bombay High Court in *K.Sudakar S.Shanbhag v ITO (2000) 241 ITR 865 (Bom)* has held that an assessee cannot be permitted to convert the reassessment proceedings as his appeal or revision in disguise and seek relief in respect of items earlier rejected or claim relief in respect of items not claimed in the original assessment unless relatable to escaped income and reagitate concluded matters. Allowance of such claims in respect of escaped income in case of reassessment has to be limited to the extent to which they reduce the income to that originally assessed. Income for the purpose of reassessment cannot be reduced beyond the income originally assessed.

   While an assessee cannot reagitate claims already assessed it is open to an assessee in reassessment proceedings to put forward claims for deduction of any expenditure which is relatable to the income which is sought to be assessed as escaped income in the reassessment proceedings. *CIT v Caixa Economica De God (1994) 119 CTR (Bom) 250*.

7. In a case, where the income by way of interest due from a wholly owned subsidiary was waived, the question arose whether such waiver, which was made after the end of the accounting year, can be accepted by the Assessing Officer. Since the income has already accrued as having become due as at the end of the accounting year and, therefore, legally recoverable irrespective of the fact whether it is actually received or not, it is income. It is so held in *Saraswati Insurance Co. Ltd. v CIT [2001] 252 ITR 430 (Delhi).* The fact that it had been subsequently waived cannot assist the assessee. It could not have been waived before it was so due and not after, as had been laid down in a number of cases including the one from the Apex Court as in *Morvi Industries Ltd*. *v CIT [1971] 82 ITR 835 (SC)*. The real income theory, it was held, would not apply to an income, which has already accrued. The theory cannot be understood in a manner to defeat the provisions of the Act.

8. Receipt is the basis of cash system of accounting. Where a taxpayer receives discounted interest for the three years in the year in which the Government bond is issued, the entire interest becomes assessable in the year of such receipt under cash system of accounting as was found in *CIT v A.R.Santhanakrishnan [2002] 256 ITR 187 (Mad)*. There can be little doubt, that if the receipt is of revenue character, the income is assessable on receipt basis under cash system. Even under mercantile system, the income is assessable, because the amount was not only received but was only receivable, when it got discounted.

9. Reinvestment benefit u/s.54 would require purchase of a house to the extent of capital gains within the period set out in the statute. Where the assessee is unable to register such purchase but all the same paid the consideration and obtained possession, there is no reason why the concession should not be given. In Balraj v CIT [2002] 254 ITR 22 (Delhi), it was pointed out that the Supreme Court had already decided this issue in the taxpayer's favour in CIT v T.N.Aravinda Reddy [1979] 120 ITR 46 (SC). It also pointed out that the registration of document is not mandatory for recognition of transfer in various contexts as for assessment of income under the head property in CIT v Podar Cement Pvt Ltd [1997] 226 ITR 625 (SC) or for depreciation in Mysore Minerals Ltd v CIT [1999] 239 ITR 775 (SC). Section 54 requires, inter alia, that the assessee should purchase property within two years from the date of transfer to avail of reinvestment benefit. Where he has so purchased and had even got it registered within such time, but made the payment to the seller after this period, the law is satisfied because the payment within the period is not one of the stipulated conditions. This view is supported in CIT v Kanta Devi Saraf [2002] 254 ITR 317 (Cal).

10. Where a property which consists of the land acquired long prior to the three year limit, but the superstructure has been put up thereon during the last three years, a question arises whether it should be treated as long term or short term capital asset. The Madras High Court in *CIT v T.C.Itty Ipe [2001] 249 ITR 591 (Mad)* has held that it should be treated as a plural sale by treating the land and building as two separate assets and computing the capital gains for the land as long term capital gains and for the superstructure as short term capital gains. This decision accords with the view taken by the Madras High Court itself earlier in *CIT v Dr.D.L.Ramachandra Rao [1999] 236 ITR 51 (Mad)* and the Rajasthan High Court in *CIT v Vimal Chand Golecha [1993] 201 ITR 442 (Raj)*.

11. Recording of reasons for initiating action for reassessment is an administrative act so that there is no need for disclosure of materials at the stage of issue of notice as was pointed out in *S.Narayanappa v CIT [1967] 63 ITR 219 (SC)*. But where the reasons are required by the assessee, he is entitled to such reasons recorded as he would not otherwise be able to effectively contest the validity of the initiation of reassessment proceedings subject to protection of Assessing Officer's sources/information, where such protection is considered necessary.

    The Supreme Court in *GKN Driveshafts (India) Ltd. v ITO [2003] 259 ITR 19 (SC)* has held that the Assessing Officer is bound to furnish the reasons within reasonable time, if the assessee asks for the same after filing a return in response to the notice and that the assessee is entitled to the same. If the assessee has any objections to the jurisdiction, he can file them. If he does, the Assessing Officer is bound to deal with them in a speaking order.

12. Dealing in shares will not be treated as a speculative transaction unless in a case where there is no delivery of such shares. Section 43(5) provides that where there is actual delivery, transactions of sale in goods and commodities including shares and scrips will not be treated as speculative

    Dealing in derivatives will not be treated as speculative transaction and the income or loss from dealing in the same will be treated as regular business income or loss if the transaction is carried on through a registered broker or sub-broker or by banks or mutual funds and where the transaction is carried out electronically on screen based systems and which is supported by a time stamp contract note which indicates the client identity and the number allotted under the SEBI Act or the SCR Act or the Depositories Act and also gives the permanent account number of the client.

PRIME ACADEMY
PROGRESS TEST
FINAL
INDIRECT TAXES

Time : 2 Hrs. **Maximum Marks : 75**

PART A

Answer 25 Questions (25 X 1 = 25 Marks)

1. Sec.3(1) of Central Excise Act 1944 speaks levying of two types of duties. They are :-
   a) Basic Excise Duty (BED) & Special Additional Duty (SAD)
   b) Basic Excise Duty (BED) & Special Excise Duty (SED)
   c) Basic Customs Duty (BCD) & Special Excise Duty (SED)
   d) Basic Customs Duty (BCD) & Special Additional Duty (SAD)

2. Sec.2(d) of the Central Excise Act defines Excisable Goods to be
   a) Goods which are specified in the Tariff as being subject to duty of excise
   b) Goods which are specified in the Act as being subject to duty of excise
   c) Goods which are given under the Rules as being subject to duty of excise
   d) None of the above

3. The word 'Manufacture' includes any process
   a) incidental or ancillary to the completion of a manufactured product;
   b) which is specified in relation to any goods in the Section or Chapter Notes of the Schedule of the Central Excise Tariff Act, 1985 as amounting to Manufacture
   c) which, in relation to the goods specified in the Third Schedule, involves packing or repacking of such goods in a unit container or labelling or re-labelling of containers includingthe declartion or alteration fo retail sale price on it or adotpion of any other treatment on the goods to render the product marketable to the consumer
   d) All of the above

4. The concept 'Place of Removal' is covered under :-
   a) Sec.4(3)(c) of the Central Excise Act
   b) Sec.4(3)(b) of the Central Excise Act
   c) Sec.4(3)(a) of the Central Excise Rules
   d) Sec.4(3)(d) of the Central excise Rules

5. Under Valuation Rules, Duty based on Value is calculated on the basis of:-
   a) Duty based on the Tariff Value
   b) Duty based ont eh value arrived at on the basis of valuation under Sec.4
   c) Duty based on Maximum Retail Price
   d) All of the above
   e) Only a & b of the above

6. Cenvat Credit Rules was introduced on
   a) 10.10.2004
   b) 9.8.2004
   c) 10.9.2004
   d) 9.7.2004

7. ‘Exempted Goods’ under Rule 2(d) of Central Excise Rules is :-
    a) Goods which are exempt from the whole of the duty of excise leviable thereon and includes goods which are chargeable to “Nil” rate of duty
    b) Goods which are exempt from the whole of the duty of excise leviable thereon but does not includes goods which are chargeable to “Nil” rate of duty
    c) Goods which are specified in the Tariff and are not subjected to duty
    d) Goods whciha re specified in the Tariff which are chargeable to “Nil” rate of duty

8. To avail SSI Exemption the turnover for the previous year should be :-
    a) Less than Rs.1 Crores
    b) Less than Rs.4 Crores
    c) Less than Rs.3 Crores
    d) Less than Rs.2 Crores

9. Cenvat Credit Rules, 2004 consists of
    a) 4 Rules
    b) 8 Rules
    c) 12 Rules
    d) 16 Rules

10. Cenvat Credit of Capital Goods is to be availed
    a) 50% of the excise duty amount during 1st year and the balance in the subsequent years
    b) 100% during the 1st year
    c) 50% during 1st year and 25% in the second year and the remaining 25% int eh third year
    d) Only after installation

11. Appeals before Commissioner of Central Excise (Appeals) against the lower authorities order have to be filed by the assessees (without condonation period) within ___ days of the receipt of the said order:
    a) 30 days
    b) 60 days
    c) 90 days
    d) 120 days

12. Excise Audit will be conducted every year for the Units paying duty :-
    a) More than Rs.3 Crores
    b) Between Rs.1 Crore and Rs.3 Crores
    c) Between Rs.50 lakhs and Rs.1 Crore
    d) More than Rs.5 Crores

13. Duration of the Excise Audit Team for the Units paying PLA over Rs.1 Crore per annum
    a) 10 working days
    b) 20 days
    c) 15 working days
    d) 7 days

14. The expansion of the word ‘CERA’ is :-
    a) Central Revenue Audit
    b) Central Excise Revenue Audit
    c) Cost Records Audit
    d) Central Regulation Audit

15. Assessees in CERA is required to produce before audit parties :-
    a) Records
    b) Cost Audit Report
    c) Income Tax Report
    d) Only (a) & (c) of the above
    e) Only (b) & (c) of the above
    f) All of the above

16. As per Sec.6 of Central Excise Act, Central Excise Registration is requried to be obtained by
    a) Every manufacturer or producer of exciseable goods
    b) Wholsesale purchase or sale or storage of any specified goods included in First and Second Schedule to Central Excise Tariff Act
    c) Both the above
    d) None of the above

17. The Term "ECC" would refer to:-
    a) Excise Classification Code
    b) Excise Control Code
    c) Exact Classification Code
    d) Excise Compliance Code

18. Registration under Central Excise is not required for :-
    a) EOU
    b) Unit in SEZ
    c) DTA
    d) None of the above

19. DSA of manufactured goods would refer to:-
    a) Daily Storage Account
    b) Daily Stock Account
    c) Duty Stock Account
    d) None of the above

20. Sec.2(a) of CEA defines "Adjudicating Authority" as
    a) Commissioner (Appeals) and Central Board of Excise and Customs
    b) Any authority competent to pass any order or decision under the Central Excise Act, 1944
    c) Both the above
    d) None of the above

21. Appeal to be preferred before CESTAT only against the Order of the :-
    a) Commissioner of Central Excise (Appeals)
    b) Commissioner of Central Excise
    c) Additional Commissioner of Central Excise
    d) All of the above
    e) Both (a) & (b) above
    f) Both (b) & (c) above

22. Commissioner (Appeals) has powers to condone the delay in filing the appeal
    a) For a further period fo 30 days
    b) For a further period of 15 days
    c) For a further period of 90 days
    d) For a further period of 60 ays

23. Appeal before High Court against CESTAT's Order can be made by the assessees if
    a) the case involves is a substantial question of law
    b) rate of duty or valuation of duty
    c) Order of the CESTAT is against the assessee on any matter
    d) All of the aobve

24. Appeal to be filed before Supreme Court should be in
    a) 4 Sets
    b) 5 Sets
    c) 6 Sets
    d) 7 Sets

25. The maximum appeal fee payable to CESTAT is
    a) Rs.5000
    b) Rs.3000
    c) Rs.1000
    d) Rs.10000

PART B

Answer any 5 (5 X 10 = 50 Marks):

1. a) Name 4 articles on which excise duty is payable at Specific Rate of Duty (2 Marks)
   b) Explain the provision in the Central Excise Act, 1944 for valuation of excisable goods with reference to retail sale price (5 Marks)
   c) Refrigerators under Heading No.8418.10 carry 'abatement rate' of 40% and they are specified only in the First Schedule to the Central Excise Tariff Act, 1985. Find out the amount of the duty, if the maximum retail price (MRP) of a refrigerator is Rs.20,000 only and the rate of excise duty is 14% plus education cess of 2% (3 Marks)

2. a) Is actual sale necessary for levy of Central Excise Duty (3 Marks)
   b) Discuss briefly with reference to provisions of Central Excise Act and any case law available, whether the following process would amount to 'manufacture'. XYZ Corporation is engaged in the process of mixing aluminum paste, metal liquor and thinner resulting in the production of aluminum paint having a shelf life of 8-10 hours.- (3 Marks)
   c) Write short note on – Manufacturer under the Central Excise Act, 1944

3. a) Briefly Explain with reference to provisions of Cenvat Credit Rules, 2004 – (3 Marks)
   b) What is Best Judgement Assessment ? (3 Marks)
   c) Prize of 'Z' is Rs.1000 if sold from the factory at Varanasi; Rs.1,150 if sold from his depot at Kolkatta and Rs.1,100 if Sold from ex-depot Kanpur. On 30th Mar., 2008 assessee dispatched pieces of 'Z' to his depot at Kolkatta. The goods reached Kolkatta Depot on 16th April 2008. The assessee increased his selling prices on 1st April 208. As per increased prices, the ex-factory prices was Rs.1,050 and ex-Kolkatta depot price was Rs.1200. The goods were actually sold from Kolkatta at Rs.1200 on 9th May 2008. What is the duty payable. Rate of excise duty is 14% plus education cess @ 2% and SAH Education Cess @ 1%. (All aforesaid prices are exclusive of taxes and duties).

      What will be the position if 90 pieces are sold from Kolkatta at Rs.1,200, four pieces are sold @ Rs.1,150 and six pieces were transferred to another depot from which they are sold later @ Rs.1,400 per piece.

4. a) What is the period of validity of the Registration Certificate granted by the Appropriate Excise Authority ? (2 Marks)
   b) Briefly examine the correctness or otherwise of the following statement with reference to the Central Excise Act, 1944 giving reasons to support your answers – Exemption from duty does not mean exemption from registration (4 Marks)
   c) A Small Scale Unit has effected clearances of goods of the Value of Rs.460 lakhs during the Financial Year 2007 -2008. The said clearances include the following : (i) Clearance of excisable goods without payment of Excise Duty to a 100% EOU Unit : Rs.40 lakhs; (ii) Export to Nepal and Bhutan : Rs.50 lakhs; (iii) Job-work in terms of Notification No.214/86-CE which is exempt from duty : Rs.60 lakhs; (iv) Goods manufactured in rural area with the brand name of others : Rs.70 lakhs. Write a brief note with reference to Notification governing SSI under the Central Excise Act whether the benefit of exemption would available to the unit for the Financial 2008 – 2009 (4 Marks)

5. a. Write Short note on – Scope of Excise Audit 2000 (6 Marks)
   b. Explain briefly the provisions relating to 'Special Audit' in certain cases under Sec.14A and Sec.14AA of the Central Excise Act, 1944 (4 Marks)

6. a. Write Short Note on the "Appellate Remedies" ((i.e) right of appeal to persons aggrieved by the Order passed an adjudicating authority) under the provisions of Central Excise Act, 1944 (3 Marks)
   b. Write short note on – Authorized Representative' (2 Marks)
   c. Which is the forum for obtaining stay of demand of duty excise confirmed by a Commissioner of Central Excise (2 Marks)
   d. What are grounds for obtaining a stay of demand of duty ? (3 marks)

PRIME ACADEMY

27th SESSION PROGRESS TEST

FINAL – INDIRECT TAXES

Suggested Answers

PART A

1. b
2. a
3. d
4. a
5. d
6. c
7. a
8. b
9. d
10. a
11. b
12. a
13. a
14. a
15. f
16. c
17. b
18. b
19. b
20. b
21. e
22. a
23. a
24. d
25. d

PART B

1. a)

a) Cigarettes (Length Basis)
b) Matches (Per 100 Boxes / Packs)
c) Sugar (per quintal basis)
d) Marble slabs and tiles (Square meter basis)
e) Colour TV when MRP is not marked on the package or when MRP is not the sole consideration (based on screen size in cm)
f) Cement Clinkers (per tonne basis)
g) Molasses resulting from extraction of sugar (Per ton basis)

{You can answer any 4 listed above}

b)

The provisions of valuation on MRP basis are as follows :-

a) The goods should be covered under provisions of Standards of Weights and Measures Act or Rules (Sec.4A(1))
b) Central Government has to issue a notification in Official Gazette specifying the commodities to which the provision is applicable and the abatements permissible. Central Government can permit reasonable abatement (deductions) from the 'retail sale price' (Sec.4A(2))
c) While allowing such abatement, Central Government shall take into account excise duty, sales taxes and other taxes payable on the goods (Sec.4A(3))
d) The 'retail sale price' should be the maximum price at which excisable goods in packaged forms are sold to ultimate consumer. It includes all taxes, freight, transport charges, commission payable to dealers and all charges towards advertisement, delivery, packing, forwarding charges etc. If under certain law, MRP is required to be without taxes and duties, that price can be the 'retail sale price' [Explanation 1 of Sec.4A].
e) If more than one 'retail sale price' is printed on the same packing, the maximum of such price will be considered [Explanation 2(a) to Sec.4A]. If different MRP are printed on different packages for different areas, each such price will be 'retail sale price' for purpose of valuation [Explanation 2(c) to Sec.4A].

f) Tampering, altering or removing MRP is an offence and goods are liable to confiscation (Sec.4A(4)). If price is altered, such increased price will be the 'retail sale price' for purpose of valuation [Explanation 2(b) to Sec.4A]/

c)

Since abatement of 40% is available, assessable value of refrigerator will be Rs.12,000 (MRP Rs.20,000 – Abatement @ 40% Rs.8,000). Basic excise duty @ 14% will be Rs.1,680. Education Cess @ 2% of Rs.1,680 is Rs.33.60. SAH Education Cess @ 1% of Rs.1,680 is Rs.16.80.

2. a)

Marketability is an essential ingredient in order to be dutiable. Marketability is a decisive test for dutiability. It only means 'saleable' or 'suitable for sale'. It need not in fact be marketed. The article should be capable of being sold to consumers, as it is without anything more.

b)

Under Excise Act, the two tests needs to be done for any process to be covered under 'manufacture'. The resultant product should be 'movable' and it is a marketable.

In the instant case, though the aluminum paint is having a short shelf life of 8-10 hours only, the paint is capable of movable and as well marketable. Therefore, it would amount to manufacture.

Further, it has been held in the case of Tamil Nadu State Transport Corporation Ltd. Vs. CCE – 166 ELT 433 (SC) that if the goods are marketable in the short shelf life, they will be 'excisable goods'.

Therefore, Aluminum Paint, will be 'excisable goods' and are subject to duty.

c)

Sec.2(f) which defines the word 'manufacturer' as 'the word manufacturer shall be understood accordingly and shall include not only a person who employs hired labour in the production or manufacture of excisable goods, but also any person who engages in their production or manufacture on his own account".

This definition is not exhaustive but inclusion. The definition enlarges definition of 'manufacturer' to two categories of persons, besides actual manufacturers namely;- a) Persons who get the goods manufactured through hired labour. b) Persons who engage in manufacture of goods on their own account. - These may be termed as 'deemed manufacturers'.

The definition of 'manufacturer' u/s.2(f) is not exhaustive. Hence, the word 'Manufacturer' is a person who actually manufactures or produces excisable goods i.e, one who actually brings into existence new and identifiable product. Raw material supplier or brand name owner is not 'manufacturer'.

3. a)

Rule 3(1) of Cenvat Credit Rules states that a manufacturer or producer of final products and a provider of output service shall be allowed to take Cenvat Credit. EOUs can also avail Cenvat Credit.

The Cenvat Credit is of specified duties (Basic, Special, AED, NCCD, Education Cess, Secondary Education Cess, Service Tax, CVD on Imported goods) paid on inputs or capital goods received in the factory or premises of service provider and also service tax paid on input services.

b)

If assessment is not possible under any of the foregoing rules, assessment will be done by 'best judgement' If the value of any excisable goods cannot be determined under the foregoing rules, the value shall be determined using reasonable means consistent with the principles and general provisions of these rules and sub-section (1) of Sec.4 of the Act.

As per the present valuation rules, there is no provision for calculating 'Value' in following cases ;- a) If assessee makes sale partly to related person and partly to others b) Free samples. In these cases, valuation may be done under Rule 11.

c)

The duty payable is on the basis of price ruling ex-depot Kolkatta on the date of removal from the factory.

Here, the date of removal is on 30th Mar.2008 and at that date, the price prevailed was Rs.1,150 – ex-depot Kolkatta.

Thus duty payable is :	14% duty on Rs.1,150	- Rs.	161
	2% Edn. Cess on Rs.161	- Rs.	3.22
	1% SAH Edn. Cess on Rs.161	- Rs.	1.61

Total duty payable on 100 pieces will be Rs.16,100 plus Edn. Cess of Rs.322 and SAH Edn. Cess of Rs.161.

Any subsequent change in prices after 30th Mar.2008 has no effect on duty payable.

4. a) The Registration Certificate is mandatory for the units operating under Excise. Therefore, the Registration Certificate is permanent unless it is cancelled by the Unit on closure.

b)

Yes. The Statement is true. Each manufacturer unless exempted from provisions of registration has to obtain registration even if he is exempt from duty. Exemption from excise duty does not mean exemption from registration.

Provisions of exemption and registration are independent of each other. Registration and compliance of following of excise procedures is necessary even if a product is exempt from duty, unless exemption from registration is granted under Rule 9(2).

Rule 9(2) of CER authorises Board to grant exemption from registration in certain cases. Notification No.36/200-CE (NT) grants exemption from registration – Thy are :- i) Persons who manufacture excisable goods which are unconditionally exempt from excise duty (ii) SSI units availing exemption based on value of clearance, whose turnover is less than the SSI exemption limit; (iii) Persons getting goods manufactured from others on his own account, if he authorises actual manufacturer to pay excise duty (iv) Persons manufacturing excisable goods under Customs Warehousing Procedures, if all their products are exported (v) Person who carries on wholesale trade or deals in excisable goods who does not issue Cenvatable Invoice (i.e) who is not a registered dealer (vi) Users of excisable goods (vii) A Unit in SEZ

c)

An SSI Unit will be entitled to SSI exemption in 2008-2009 only if its turnover in 2007-2008 is less than Rs.400 lakhs. While calculating the turnover of Rs.400 lakhs, the following are not required to be considered :-

a) Deemed Exports (i.e) Supplies to EOU

b) Job work that amounts to 'manufacture' done under Notification No.214/86-CE, 83/94-CE and 84/94-CE.

Exports to Nepal and Bhutan cannot be excluded, i.e, export turnover to Nepal and Bhutan will have to be added while calculating limit of Rs.150 and Rs.400 lakhs. It will be treated as 'clearance for home consumption', even if actually it is 'export'. The export to Nepal and Bhutan will be includible even if such export is against free foreign exchange.

If goods are manufactured in rural area with other's brand name, these are exempt upto Rs.150 lakhs. In such case, that turnover which is cleared without payment of duty will have to be included for calculating exemption limit of Rs.400 lakhs.

Thus, turnover in respect of sale to EOU (Rs.40 lakhs) and job work under notification No.214/86-CE (Rs.60 lakhs) is required to be excluded for purpose of SSI Exemption limit of Rs.400 lakhs. Turnover of SSI excluding these sales is Rs.360 lakhs (Rs.460-40-60 lakhs). Hence, SSI Unit will be entitled to exemption in 2008-2009 upto first turnover of Rs.150 lakhs.

5. a.

Most of the Factories are under 'Self Removal Procedure' and there is no physical control over production and clearance of goods. Department has evolved various checks and counter checks to ensure that excise duty is not evaded. Following checks have been devised to reduce leakage of revenue.

<u>Scrutiny of returns</u> – Every assessee, first stage dealer and second stage dealer has to submit periodic returns to Superintendent of Central excise. This will be acknowledged by him on the assessee's copy. No assessment order will be issued. These returns will only be scrutinised. Further enquire can be made as provided in rule 12(3).

<u>Visits of Officers</u> – Every factory comes under jurisdiction of Range Superintendent. The Superintendent and Excise Inspectors working under him do occasionally visit factories. However, they are not expected to have day to day checks.

<u>Stock taking</u> – Present Central Excise Rules make no provision for 'store room' or 'stock taking'. However, it does not mean that stock taking by excise authorities is prohibited. Stock taking can be done of finished goods and Cenvat goods.

<u>Road Checks</u> – Surprise road checks are carried out to see that all goods moving are accompanied by duty paying documents.

<u>Information from Informants</u> – Like all tax departments, department can and does collect information from secret informants.

<u>Preventive Section</u> - Each Commissionerate has a preventive section to have surprise checks and raids and when evasion is suspected.

<u>Central Excise Intelligence</u> - Directorate of Central Excise Intelligence under Central Board of Excise and Customs gathers information from various sources (including information about tax evasion and take suitable action). The officers have been given powers on all India basis.

b.

Sec.14A and Sec.14AA make provision for Special Audit by Cost Accountants.

<u>Valuation Audit – Special Audit</u> – Valuation is one of the most vital and important aspect of assessment of excise duty payable. In order to ensure that duty is being paid on correct 'Assessable Value', a provision has been made to order a 'Special Audit' in some specified cases vide Sec.14A of CEA. The audit can be ordered only with prior approval of Chief Commissioner of CE.

<u>Cenvat Credit Audit – Special Audit</u> – As per Sec.14AA of CEA, special audit of Cenvat Credit availed or utilised can be ordered by Commissioner of Central Excise. Such audit can be ordered if the Commissioner of Central Excise has reason to believe that (a) Cenvat Credit availed or utilised is not within the normal limits, having regard to nature of final products and type of inputs (b) Cenvat credit has been availed or utilised by reason of fraud, collusion or any willful misstatement or suppression of facts.

Such audit can be done by practicing 'Cost Accountant' to be appointed by Commissioner of Central Excise. Expenses of and incidental to such audit, including remuneration payable to the cost accountant shall be paid by Central Excise Government (i.e, Excise Department).

6. a. Excise law empowers excise officers to pass adjudication orders demanding duty and interest and imposing penalty and confiscation of goods.

Excise Act have made elaborate provisions for appeals against adjudication orders passed by excise authorities.
There is only one appeal before the Tribunal – CESTAT in case of Order of the Commissioner.

While in case of other Orders (i.e., Orders of Superintendent, Assistant Commissioner, Dy. Commissioner, Jt. Commissioner, Additional Commissioner) first appeal with Commissioner (Appeals) and other with Tribunal.
In some cases, revision application lies with Government against orders of Commissioner and Commissioner (Appeals).

Tribunal is final fact finding authority and no furhter appeal against facts as found by Tribunal. In case of order of Tribunal relating to classification or valuation, appeal lies with Supreme Court. In other matters, appeal can be made to High Court only if substantial question of law is involved.

b.

As per Sec.35Q(2) of CEA, the authorised representative may be (a) Relative of a Person appearing or a regular employee b) Advocate who is authorised to practice in Civil Court c) Persons holding requisite qualification prescribed under rule 12 of Central Excise (Appeals) Rules

c.

CESTAT – Central Excise and Service Tax Appellate Tribunal is the forum which can grant stay of recovery if order of demand of duty and imposition of penalty is passed by Commissioner of Central Excise or Commissioner of Central Excise (Appeals)l.

d.

There are two grounds based on which stay is granted. They are:-

<u>Prima facie case :</u>
If strong prima facie case is made out, deposit of duty and penalty may be dispensed with or considerably reduced, even if no financial hardship is pleaded. Thus factors like (a) not considering decisions of Courts in the issue by lower authority (b) order without jurisdiction (c) not following principles of natural justice by lower authority (d) order based on no evidence etc. can be considered

<u>Financial Hardship :</u>
Adequate bank guarantee and solvent surety is obtained to secure interest of revenue, while not crippling the person by asking to make payment, which he may not be able to do financially. Balance Sheet and various other factors are to be considered.