PRIME ACADEMY
38TH SESSION PROGRESS TEST
ADVANCED MANAGEMENT ACCOUNTING

No of pages: 5 **Total Marks: 75**
Time Allowed: 2Hrs

Part - A

I. Indicate the correct answer from the options given. Show workings/reasons briefly in support of your answer

1. The use of contribution per unit of limiting factor as the basis for ranking products to be produced and sold is aimed at which of the following?
   (a) Maximization of turnover (b) Maximization of long-term profit
   (c) Maximization of labour employed (d) Maximization of short-term profit

2. A cost incurred in the past and hence irrelevant for current decision making is
   (a) Fixed cost (b) Discretionary cost
   (c) Sunk cost (d) Direct cost

3. A Company temporarily has excess production capacity. The idle plant facilities can be used to manufacture a low-margin item. This item should be produced if it can be sold for more than its
   (a) Fixed costs (b) Variable costs
   (c) VC+ opportunity cost of idle facilities (d) Total costs + opportunity cost

4. Contribution Approach is a method of preparing income statement that separates variable cost from Fixed Cost to emphasize cost behavior pattern for the purpose of planning and control.
   (a) True
   (b) False

5. A retail company sells computers, each of which is sold for ₹ 250 and bought from the manufacturer for £100. The retailer's fixed costs are ₹ 150,000. Maximum possible sales are ₹ 3,000. How many computers must be sold to break-even?
   (a) 2,000
   (b) 1,000
   (c) 3,000
   (d) 750

6. In the above question, how many computers would have to be sold for the company two and a profit of ₹ 180,000?
   (a) ₹ 1,200
   (b) ₹ 1,000
   (c) ₹ 720
   (d) ₹ 2,200

7. A company makes and sells a single product. The selling price and marginal revenue equations are: SP = ₹ 50 –₹0.001X; Marginal Revenue = ₹50 – ₹0.002X; Where X is the product the company makes. The variable costs amount to ₹ 20 per unit and the fixed costs are ₹ 1,00,000. In order to maximize the profit, the selling price should be
   (a) ₹ 25
   (b) ₹ 30
   (c) ₹ 35
   (d) ₹ 40

8. A company has budgeted break-even sales revenue of ₹ 8,00,000 and fixed costs of ₹ 3,20,000 for the next period. The sales revenue needed to achieve a profit of ₹ 50,000 in the period will be
   (a) ₹ 8,50,000
   (b) ₹ 9,25,000
   (c) ₹ 11,20,000
   (d) ₹ 12,00,000

9. A 'Margin of Safety' is the total production a factory can make in a financial period. State reason
   (a) True
   (b) False

10. If contribution per unit is ₹ 3, 9,000 units are sold for ₹ 7 each and Fixed Costs are ₹ 6,000, the maximum profit is ₹ 21,000. State reason
   (a) True
   (b) False (10 x 2 = 20 Marks)

II. Fill in the blanks

11. Marginal Cost is a ____________ratio which may be expressed in terms of an amount per unit of output.
12. The _____________ of funds invested in a business is the interest that could have been earned by investing the funds in bank deposit
13. When management is faced with a problem as to whether a particular part should be manufactured or bought in the market, two factors are to be considered. One is whether surplus capacity is available and two _____________
14. The disposal value of equipment is ___________ because it adds to the cash inflow arising from the decision.
15. _________ measures the relationship of contribution, the relative profitability of different products, processes or departments. (5 x 1 = 5 Marks)

Part-B **(50 Marks)**

Answer any 4 questions

(Each Qn. Carry 12.5 Marks)

1. A company has a capacity of 40,000 hours per annum for manufacture of four components required for assembly of a product. The data (in ₹)are as under:

Components	**P ₹**	**Q ₹**	**R ₹**	**S ₹**
Materials	64.75	47.25	43.75	77.00
Labour (₹8.75/hr)	17.50	35.00	17.50	105.00
Direct expense	17.50	14.00	38.50	70.00
Fixed Overheads	8.75	7.00	19.25	35.00

The data relating to the number of components required per annum and the prices of the components, if purchased from the market, are as under:

	P ₹	**Q ₹**	**R ₹**	**S ₹**
No. of components required	2400	4800	1200	2400
Purchase price per component (`)	105	103	91	294

If the company resorts to working a second shift to manufacture its requirement of components, it will increase the labour costs by 25% over normal shift. In addition, the fixed costs will increase by ₹ 875 per 1000 hours or part thereof of second shift working.

(i) Prepare statements to show which of the components and in what quantities should be manufactured in 40,000 hours

(ii) Whether it will be profitable to manufacture any balance quantity of components by second shift operation

2. A company produces three products and is reviewing the production and sales budgets for the next accounting period. Following information is available for the three products:

	Product X	**Product Y**	**Product Z**
Contribution p.u	₹ 12	₹ 10	₹ 6
Machine hours required p.u	6 hrs	2 hrs	1 hr
Estimated sales demand	200 units	200 units	200 units
Required machine hrs	1200 hrs	400 hrs	200 hrs

Machine capacity is limited to 1200 hours and is insufficient to meet total sales demand

(i) You have been asked to advise as to which product should be produced during the period. Compute total contribution.

(ii) State one assumption in which products mix advised by you in (i) based on contribution per unit of limiting factor will not hold good.

3. Price Ltd manufactures Product 'S' in departments A and B which also manufacture other products using the same machine. The particulars per unit of the product 'S' are as under:

Direct Material	M - 8 kgs at ₹ 3 per kg used in dept A P - 4 Kgs at ₹ 5 per kg used in dept B	
Direct labour	2 hours at ₹ 12 per hour in dept A 3 hours at ₹ 10 per hour in dept B	
Overheads (method of recovery)	Dept A and B – direct labour hours	
Overhead rates:	**Dept A**	**Dept B**
Fixed	₹ 6 per hour	₹ 3 per hour
Variable	₹ 5per hour	₹ 2 per hour
Value of Plant & machinery	₹ 16 lakhs	₹ 8 lakhs

Variable selling and distribution overheads relating to Product ‘S’ amount to ₹20,000 per month. The product requires a working capital of ₹3,00,000 at the target volume of 1000 units per month occupying 25% of the practical capacity. Required:

(i) Using the return on investment pricing formula, find the price of Product ‘S’ to yield a contribution to cover 24% rate of return on investment.

(ii) If Product ‘S’ is a well-established product in the market, what should be the basis for fixation of price. Set the minimum price on that basis.

4. XYZ Co. has received an once-off export order for its sole product that would require the use of half of the factory’s total capacity, which is estimated at ₹ 4 Lakhs units/annum. The condition of the export order is that it has to be accepted in full; acceptance of part quantity is not allowed. The factory is currently operating at 60% level to meet the demands of its domestic customers. As against the current price of ₹ 6/- per unit, the export offer is ₹ 4.70/unit, which is less than the total cost of the current production. The cost breakdown is given below:

	₹/unit
Direct material	2.50
Direct labour	1.00
Variable expenses	0.50
Fixed overhead	1.00
Total Cost	5.00

The company has the following options:

(a) Accept the export order and cut back domestic sales as necessary.

(b) Remove the capacity constraints by installing necessary balancing equipment and also by working overtime to meet both domestic and export demand. This will increase fixed overhead by ₹ 15,000 annually and additional cost for overtime work will amount to ₹ 40,000 for the year.

(c) Appoint a sub-contractor to manufacture the additional requirement and meet the domestic & export requirements in full by supplying the raw materials, paying a conversion charge@ ₹2 per unit and appointing a supervisor at a salary of ₹ 3,000 per month for checking the quality of the product and controlling operations at the manufacturing unit.

(d) Refuse the export order.

Required:

(i) A statement of costs and profits under each of the above 4 options.

(ii) Your recommendation, with reasons, as to which of these options the company should decide upon.

5. A sports goods manufacturer, in conjunction with a software house, is considering the launch of a new sporting simulator based on videotapes linked to a personal computer enabling much greater realism to be achieved. Two proposals are being considered. Both use the same production facilities and, as these are limited, only the product can be launched. The following data are the best estimates the firm has been able to obtain:

	Football simulator	**Cricket simulator**
Annual volume (units)	40,000	30,000
Selling price	₹ 130 per unit	₹ 200 per unit
Variable production costs	₹ 80 per unit	₹ 100 per unit
Fixed production costs	₹ 6,00,000	₹ 6,00,000
Fixed selling and administrative costs	₹ 4,50,000	₹ 13,50,000

The higher selling and administration costs for the cricket simulator reflect the additional advertising and promotion cost expected to be necessary to sell the more expensive cricket system. The firm has a minimum target of ₹ 2,00,000 profit per year for new products. The management recognizes the uncertainty in the above estimates and wishes to explore the sensitivity of the profit on each product to changes in the values of the variable (volume, price, variable cost per unit, fixed costs)

You are required:

(i) To calculate the expected profit from each product;

(ii) To calculate the critical value for each variable (i.e., the value at which the firm will earn ₹ 2,00,000), assuming that all other variables are as expected (express this as an absolute value and as percentage change from the expected value).

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SUGGESTED ANSWERS

PART A

1. (d) Maximization of short-term profit
2. (c) Sunk cost
3. (b) Variable costs
4. (a) True
5. (b) 1000
6. (d) 2200
7. (c) ₹ 35

   Selling price = ₹ (50-0.001 X)

   Marginal revenue = ₹ (50-0.002 X)

   Variable cost per unit = Marginal cost per unit = ₹ 20

   Optimal output for maximum profit: 20 = 50 – 0.002 X

   Whence, x = 30/0.002 = 15,000 units

   SP = 50 – 0.001 X

   = 50 – 0.001 (15,000) = ₹ 35
8. (b) ₹ 925,000
9. (b) False
10. (a) True; Total contribution at maximum sales = 9,000 x ₹ 3 = ₹ 27,000, less Fixed Costs ₹ 6,000 = ₹ 21,000.

11. Variable cost
12. Opportunity cost
13. Marginal cost
14. Relevant
15. Marginal costing

PART B

1)

	P ₹	**Q** ₹	**R** ₹	**S** ₹
Direct Wages	17.50	35	17.50	105
Direct labour hrs @ ₹ 8.75p.h	2	4	2	12
Variable mfg costs	99.75	96.25	99.75	252
Purchase price	105	103	91	294
Saving if components are manufactured	5.25	6.75	-	42
Saving per hour	2.625	1.688	-	3.50
Ranking	2	3	-	1

(i) Statement showing product-mix of the components to be manufactured (Available hrs 40,000)

Component	Qty reqd ₹	Hrs/unit ₹	Production ₹	Hrs used ₹	Balance hrs ₹
S	2400	12	2400	28800	11200
P	2400	2	2400	4800	6400
Q	4800	4	1600 (6400/4)	6400	-

Components to be purchased

Q ₹ 3200

R ₹ 1200

(ii) Statement showing impact of second shift working

		₹
Additional quantity of Q required	3200	
Hours required to manufacture (3200*4)	12800	
Fixed cost (₹ 875/1000)*13000	(11375/3200)	3.55
Increase in labour cost (₹ 35*25%)		8.75
Total		**12.30**
Saving in cost		6.75
Loss if component Q is manufactured		**5.55**

Hence II shift operation is not recommended

2)

(i)

	X	Y	Z
Contribution p.u	₹ 12	₹ 10	₹ 6
Machine hrs reqd p.u	6	2	1
Contribution per machine hr	₹ 2	₹ 5	₹ 6
Ranking	3	2	1

Step 1: First 200 units of Product Z should be produced utilizing 200 hrs and leaving 1000 unutilized hours as contribution per unit of machine hour is highest in the case of product Z

Step 2: 200 units of product Y should be produced utilizing 400 hrs and leaving 600 machine hrs still unutilized

Step 3: 600 available machine hrs should be utilized for Product X producing 100 units

Product Mix

Production	Machine hrs used	Balance
200 units of Z	200	1000
200 units of Y	400	600
100 units of X	600	-

This production will yield highest total contribution as follows:

200 units of Z * ₹ 6	₹1200
200 units of Y * ₹ 10	₹2000
100 units of X * ₹ 12	₹ 1200
Total contribution	**₹4400**

(ii) It is necessary to consider other qualitative factors before the proposed production program is implemented. For example, customer goodwill will be lost causing a fall in future sales if company is unable to supply all three products to say, 150 of its regular customers. Company's relation with customer may at times compel the management to take a sub-optimal decision in a temporary situation.

3)

(i) Based on return on investment

	₹
Direct material	
M – 8kg x ₹ 3	24
P-4 kg x ₹ 5	20
Direct labour	
Dept A – 2 hrs x ₹ 12	24
Dept B – 3hrs x ₹ 10	30
Variable overheads	
Dept A – 2hrs x ₹ 5	10
Dept B – 3 hrs x ₹ 2	6
Selling overhead (₹ 20000/1000)	20
Total Variable cost p.u	134

Total hrs required for a target of 1000 units of product S

Dept A – 1000 x 2 hrs	2000 hrs
Dept B – 1000 x 3 hrs	3000 hrs
Total	**5000 hrs**

5000 hrs represent 25% capacity

Per month capacity	20000 hrs
Per annum capacity	240000 hrs

Fixed capital employed in both departments

	₹
Dept A	16 lac
Dept B	8 lac
Total	**24 lac**

24% return required on an investment of ₹ 24 lacs = 24,00,000 x 0.24 = ₹ 576,000

Contribution required per hour = ₹ 576,000 / 240,000 = ₹ 2.40 for using machines in Dept A and B
Working capital = ₹ 300,000

24% return required = ₹ 300,000 /0.24 = 72000

Contribution required p.u = ₹ 72,000/12000 units = ₹ 6

Total contribution required p.u = ₹ 72,000/12000 units = ₹ 6
To cover fixed cost for usage of machinery = 5hrsx ₹ 2.40 ₹ 12 p.u
To cover working capital ₹ 6
₹ 18 p.u
Price of product S = Variable cost + contribution required = ₹ 134/₹ 18 = ₹ 152p.u

(ii) Basis if product is well established

Variable cost	₹ 134
Fixed cost	
Dept A – 2 hrs x 6	₹ 12
Dept B – 3 hrs x 3	₹ 9
	155

If the product is well established, the cost (absorption cost basis) should form the basis for price fixation. Minimum price = ₹ 155 p.u

4 **Working Notes:**

Calculation of Variable Cost/unit. ₹

Direct Material	2.50
Direct Labour	1.00
Variable expenses	0.50
Variable cost/unit	4.00

Fixed cost (at 60% level) = 4,00,000 units × 60/100 × ₹ 1 per unit = ₹ 2,40,000

Option (a): Profitability Statement (Accept export order and cut back domestic sales as necessary)

	₹
Sales : Export (2,00,000 units @ ₹ 4.70)	9,40,000
Domestic (2,00,000 @ ₹6.00)	12,00,000
	21,40,000
Less : Variable cost (4,00,000 units @ ₹ 4)	16,00,000
Contribution	5,40,000
Less : Fixed Overhead	2,40,000
Profit	3,00,000

Option (b): Profitability Statement (Installation of balancing eqpt. & increase capacity to meet both domestic and export demand)

	₹	₹
Sales: Export (2,00,000 units @ ₹4.70)		9,40,000
Domestic (2,40,000 @ ₹ 6.00)		14,40,000
		23,80,000
Less : Variable cost (4,40,000 units @ ₹ 4)	17,60,000	
Overtime payment	40,000	18,00,000
Contribution		5,80,000
Less : Fixed Overhead	2,40,000	
Extra Fixed Cost	15,000	2,55,000
Profit		3,25,000

Option (c): Profitability Statement (Sub contracting)

	₹	₹
Sales (in Option b)		23,80,000
Less : Variable Cost (4,00,000 units @ ₹ 4)	16,00,000	
Sub-contract charges :		
Material (₹ 2.50 × 40,000 units)	1,00,000	
Conversion (₹ 2.00 × 40,000 units)	80,000	17,80,000
Contribution		6,00,000
Less : Fixed overheads	2,40,000	
Supervision charges	36,000	2,76,000
Profit		3,24,000

Option (d): Profitability Statement (Refuse Export Order)

	₹
Sales : Domestic (2,40,000 units × ₹ 6.00)	14,40,000
Less : Variable Cost (2,40,000 units × Rs 4.00)	9,60,000
Contribution	4,80,000
Less Fixed cost	2,40,000
Profit	2,40,000

Analysis:

From the above, it is observed that the Profit is maximum, by installation of balancing equipment and increasing capacity to meet both domestic as well as export order. Hence option (b) is recommended.

5) (a)

Expected Profit	**Football simulator ₹**	**Cricket simulator ₹**
Volume per annum (units)	40,000	30,000
Selling price per unit	130	200
Less : Variable costs	80	100
Contribution per unit	50	100
Total contribution	20,00,000	30,00,000
Less : Total fixed costs	10,50,000	19,50,000
Total expected profit	9,50,000	10,50,000

(b) Critical factor, i.e., minimum target profit per annum on new product ₹ 2,00,000

(i) Sensitivity due to change in volume

Volume = (Fixed Cost +Profit)/Contribution per unit

Football = (₹10,50,000 + 2,00,000) / 50 = ₹ 25,000 or 37.5%*

Cricket = (₹ 19,50,000 + 2,00,000) / 100 = ₹ 21,500 or 28.3%

*(40,000 -25,000) / 40,000 = 37.5%; other percentage calculated similarly.

(ii) Sensitivity due to change in price

Price = (Fixed Cost + Profit + Variable Cost) / Volume

Football: (₹ 10,50,000 + 2,00,000 + 32,00,000) / 40,000 = ₹ 111.25 or 14.4%

Cricket : (₹ 19,50,000 + 2,00,000 + 30,00,000) / 30,000 =₹ 171.67 or 14.2%

(iii) Sensitivity due to change in variable cost per unit

Variable cost per unit = (Volume*Price-Fixed cost)/Profit

Football = (₹ 40,000 × 130 – 10,50,000 – 2,00,000) / 40,000 =₹ 98.75 or 23.4%

Cricket = (₹ 30,000 × 200 – 19,50,000 – 2,00,000) / 30,000 = ₹ 128.33 or 28.3%

(iv) Sensitivity due to change in fixed costs

Football : ₹ 20,00,000 – 2,00,000 = ₹ 18,00,000 or 71.4%

Cricket : ₹ 30,00,000 – 2,00,000 = ₹ 28,00,000 or 43.6%

The most critical factor is the price per unit, only 14% variation being sufficient to reduce profit to ₹ 2,00,000. The most critical factors are for the football, the variable cost per unit (23.4%), and for cricket the volume (28.3%) and the variable cost per unit (28.3%). The other factors are the growth potential of the two products, possible export sales, quality of the estimates, reaction of competitors etc.

PRIME ACADEMY

38th SESSION PROGRESS TEST

INFORMATION SYSTEM CONTROL AND AUDIT

No of Pages: 2 **Total Marks: 75**

Time Allowed: 2Hrs

Part -A

1) The ________ can be thought of as a set of activities that analysts, designers and users carry out to develop and implement an information system.
2) A ________ is undertaken when users come across a problem or opportunity and submit a formal request for a new system to the MIS department.
3) _______ is done to ensure that the software does not fail i.e. it runs according to its specifications and in the way users expect.
4) Specific reports and other documentation, called _________ must be produced periodically during systems development to make development personnel accountable for faithful execution of system development tasks.
5) The top management level ________ consists of a group of key IS services users that acts as a review body for IS plans and applications development
6) __________ are assigned to determine user requirements, design the system and assist in development and implementation activities.
7) _______ involves examining organisation charts and studying written operating procedures to learn about the organisation involved in, or affected by, the project.
8) A _________ is a computer file that contains descriptive information about the data items in the files of a business information system.
9) ________ use a network form to document the complex conditional logic involved in choosing among the information processing alternatives in a system.
10) _______ refers to the actual pieces of data included among the outputs provided to users.
11) ________ are sub-divisions of the display screen that make it possible to present different sets of output simultaneously.
12) The process of __________ a program refers to correcting programming language syntax and diagnostic errors so that the program "compiles cleanly".
13) A ____________ is a mental execution of the program by the programming team.
14) A _________ is a usable system or system component that is built quickly and at a lesser cost, and with the intention of being modifying or replacing it by a full-scale and fully operational system.
15) COBIT stands for __________
16) __________ is a formal testing of the operational system conducted to confirm that user requirement specifications have been met
17) _________ subjects the system to heavy volumes of data to test whether it can handle the volume of data specified in a acceptable time-frame

18) The primary objective of ______ control techniques is to prevent, detect, and correct errors in transactions as they flow through the various stages of a specific date processing program.

19) ________ are the system-based mechanisms used to designate who or what is to have access to a specific system resource

20) _______ involves the change of data before or as they are entered into the system.

21) A ________ involves forging one's source address
22) _________ is the art or science of keeping messages secret.

23) PKI stands for ____________

24) A _________ is a piece of hardware or software program which protects a computer or network from attacks from intruders and hackers.

25) VPN refers to ____________ (25 X 1=25 Marks)

Part - B **(50 Marks)**

Answer any five Questions

1)

a) Distinguish between Hackers and Crackers (4 Marks)

b) Write short notes on the following

i) Scanners

ii) Active Monitor and Heuristic Scanner

iii) Integrity Checkers (3 X 2= 6 Marks)

2)

a) As an IS auditor, how would you evaluate the physical access controls? (Role of an IS auditor in Physical Access Control) (6 Marks)

b) Write short notes on (2 X 2= 4 Marks)

i) Preventive controls

ii) Detective controls

3)

a) What are audit trails? What are the uses of such trails? (5 Marks)

b) What are the components of change management control policies & procedures? (5 Marks)

4)

a) State any 5 reasons as to why an organisation fails to achieve system development objectives? (5 Marks)

b) Write short notes on system development team (5 Marks)

5)

a) Write short notes on Operational feasibility (5 Marks)

b) What are the factors to be considered while designing system inputs? (5 Marks)

6)

a) Write short notes on systems manual (5 Marks)

b) What are the advantages to buying ready-made or pre-written application packages when compared to in-house developed software? (5 Marks)

PRIME ACADEMY

38TH SESSION PROGRESS TEST

INFORMATION SYSTEM CONTROL AND AUDIT

SUGGESTED ANSWERS

PART- A

1) System development life cycle
2) Preliminary Investigation
3) Systems Testing
4) Deliverables
5) Steering Committee
6) Systems Analysts
7) Reviewing Internal Documents
8) Data Dictionary
9) Decision Trees
10) Content
11) Windows
12) Debugging
13) Structured Walkthrough
14) Prototype
15) Control Objectives for information and related technology
16) Acceptance Testing
17) Volume testing
18) Data Integrity
19) Logical access controls
20) Data diddling
21) Spoofing Attack
22) Cryptography
23) Public Key Infrastructure
24) Firewall
25) Virtual Private Network

Part - B

1 a)

Hackers	Crackers
The computer hackers actually trespass or circumvent computer system with a hunger to know the programmable systems, how they perform and their internal structures. Hackers are most often programmers. As such, hackers obtain advanced knowledge of operating systems and programming languages. They might discover holes within systems and the reasons for such holes. Hackers constantly seek further knowledge; freely share what they have discovered, and never intentionally damage data.	A cracker is one who breaks into or otherwise violates the system security & integrity of remote machines with malicious intent. Having gained unauthorized access, crackers destroy vital data, deny legitimate users service, install several programs, steal personal information such as passwords and credit card information or cause problems for their targets. Crackers can easily be identified because their actions are malicious.

b)

i) Scanners: The software looks for a sequence of bits called virus signatures that are characteristic of virus codes. They check memory, disk boot sectors, executables and systems fillies to find matching bit patterns. It is necessary to frequently update the scanners with the data on virus code patterns for the scanners to be reasonably effective.

ii) Active Monitor and Heuristic Scanner: This looks for critical interrupt calls and critical operating systems functions such as OS calls and BIOS calls, which resemble virus action. However this also makes them inefficient since they cannot differentiate between genuine systems calls and virus action. These could be annoying and generally do not serve the purpose.

iii) Integrity Checkers: These can detect any unauthorized changes to files on the system. They require the software to "take stock" of all files resident on the system and compute a binary check data called the Cyclic Redundancy Check (CRC). When a program is called for execution, the software computes the CRC again and checks with the parameter stored on the disk. However, such checks assume that frequent changes to applications and systems utilities do not occur.

2 a)

Auditing physical access requires the auditor to review the physical access risk and controls to form an opinion on the effectiveness of the physical access controls. This involves the following:

i) Risk assessment: The auditor must satisfy himself that the risk assessment procedure adequately covers periodic and timely assessment of all assets, physical access threats, vulnerabilities of safeguards and exposures there from.

ii) Controls assessment: The auditor based on the risk profile evaluates whether the physical access controls are in place and adequate to protect the IS assets against the risks.

iii) Planning for review of physical access controls. It requires examination of relevant documentation such as the security policy and procedures, premises plans, building plans, inventory list and cabling diagrams.

iv) Testing of controls: The auditor should review physical access controls to satisfy for their effectiveness. This involves:

- Tour of organizational facilities including outsourced and offsite facilities.
- Physical inventory of computing equipment and supporting infrastructure.
- Interviewing personnel can also provide information on the awareness and knowledge of procedures.
- Observation of safeguards and physical access procedures. This would also include inspection of core computing facilities, computer storage rooms, communication closets, backup and off site facilities, printer rooms, disposable yards and bins, inventory of supplies and consumables, entry / exit points, glass windows and walls, movable and modular cubicle, ventilation and air-conditioning ducts, false ceilings and flooring panels.

v) Review of physical access procedures including user registration and authorization, authorization for special access, logging, review, supervision etc.

vi) Employee termination procedures should provide withdrawal of rights such as retrieval of physical devices like smart cards, access tokens, deactivation of access rights and its appropriate communication to relevant constituents in the organization.

vii) Examination of physical access logs and reports which includes examination of incident reporting logs, problem resolution reports.

b)

a) Preventive Controls: Preventive controls are those inputs, which are designed to prevent an error, omission or malicious act occurring. The broad characteristics of preventive controls are:
   - A clear-cut understanding about the vulnerabilities of the asset
   - Understanding probable threats
   - Provision of necessary controls for probable threats from materializing

   Some examples of preventive control are Employ qualified personnel, Segregation of duties, Access control, Documentation, Training and retraining of staff, Firewalls etc

b) Detective Control: These controls are designed to detect errors, omissions or malicious acts that occur and report the occurrence. The main characteristics of such controls are as follows:
   - Clear understanding of lawful activities so that anything which deviates from these is reported as unlawful, malicious, etc.
   - An established mechanism to refer the reported unlawful activities to the appropriate person or group
   - Interaction with the preventive control to prevent such acts from occurring
   - Surprise checks by supervisor

   Some examples include hash totals; duplicate checking of calculations, internal audit functions, Intrusion detection system, cash counts and bank reconciliation, monitoring expenditures against budgeted amount etc

3 a)

Audit trails:

Audit trails are logs that can be designed to record activities at the system, application, and user level and thus help achieving security policy objectives of the organization. Logs provide valuable evidence in assessing both the adequacies of controls in place and the need for additional controls. Many operating systems allow management to select the level of auditing to be provided by the system. An effective audit policy will capture all significant events without cluttering the log with trivial activity. Audit trails can be used to support security objectives in three ways:

- Detecting unauthorized access which can occur in real time or after the fact. Real time detection is used to protect the systems from malicious users and report on changes in system performance that may indicate infestation by a virus or worm. Logging all activities can impose a significant overhead on the operating system, and degrade operational performance. After-the-fact detection logs can be stored electronically and reviewed periodically or as needed. When properly designed, they can be used to determine if unauthorized access was accomplished, or attempted and failed.
- Audit trails can also be used to reconstruct events that result in system failures, security violations by individuals, or application processing errors. Knowledge of the conditions that existed at the time of a system failure can be used to assign responsibility and to avoid similar situations in the future.
- Personal Accountability: Audit trails can be used to monitor user activity at the lowest level of detail. Individual are likely to violate an organization's security policy if they know that their actions are recorded in an audit log.

b)

Formal change management control policies and procedure should include the following:

- Periodic review of all systems for changes, submission of user requests in a standardized format, maintaining a log of all requests, categorizing and ranking all changes using established priorities
- Audit trails and specific procedures implemented to handle urgent matter that required deviations from standard procedures and having management review and approve them after the fact
- Communication all changes to management and users on the status of their requested changes.
- Require IT management to review, monitor, and approve all changes to hardware, software, and personnel responsibilities. Ensure assigning specific responsibilities and segregation of duties for those involved in change management.
- Control 'system access rights' to avoid unauthorized systems and date access.
- Make sure all changes go through the appropriate pre-defined steps
- Test all changes in a separate, non production environment before placing it into live production mode.
- Ensure the existence of back-up plans for mission critical application changes
- Implement a quality assurance function to ensure that all standards and procedures are followed and communicate the same to the user department and the top management.
- Update all documentation and procedures when changes are implemented

4 a)

- Lack of senior management support for and involvement in information systems development.
- Shifting user needs: Constant changes results in more requests for systems development & new project which serves as a challenge to the development team
- Difficulty in defining the requirements, specifications, and objectives for development of strategic systems where the decision making is unstructured
- Personnel are not as familiar with the new technology
- Lack of standard project management and systems development methodologies
- Overworked or under-trained development staff.
- Resistance to change: People have a natural tendency to resist change, when they perceive that the project will result in personnel cutbacks such as downsizing

- Lack of user participation in the development efforts to define their requirements
- Inadequate testing and user training.

b)

Several people in the organisation are responsible for systems development. Their roles are as follows:

- The top management level steering committee consists of a group of key IS services users that acts as a review body for IS plans and applications development. The steering committee ensures that ongoing systems development activities are consistently aimed at satisfying the information requirements of managers and users within the organisation.
- If the project appears worthwhile to the steering committee, it becomes the responsibility of the IS department to develop it successfully.
- A project management team generally consisting of both computer professionals and key users is appointed to coordinate development activities of the system.
- Systems analysts are assigned to determine user requirements, design the system and assist in development and implementation activities.
- Systems designers take a lead role during the design, development and implementation stages.

In end-user developed systems, the end-user seeks guidance from information centre personnel while developing the system. Some organisations require the information centre to certify the final system as a quality assurance measure.

5 a)

Operational feasibility:

It is concerned with ascertaining the views of workers, employees, customers and suppliers about the use of computer facility. Lack of support can cause an otherwise efficient system to miserably fail.

Issues considered include:

- Is there sufficient support for the system from management and users?
- Have the users been involved in planning and development of the project? Early involvement reduces the chances of resistance to the system
- Are current business methods acceptable to users?
- Will the proposed system cause harm? Will it produce poorer results in any respect or area? Will loss of control result in any areas? Will accessibility of information be lost?
- Will individual performance be poorer after implementation than before? Will performance be affected in an undesirable way? Will the system slow performance in any areas?

b)

Input design consists of developing specifications and procedures for data preparation, developing steps which are necessary to put transactions data into a usable form for processing, and data-entry, issues to consider for design of input specifications. Factors to be considered are:

- Content: The analyst is required to consider the types of data that are needed to be gathered to generate the desired user outputs. New systems often mean new information and new information often requires new sources of data, the data needed for a new system are not available within the organisation. Hence, the system designer has to prepare new documents for collecting such information.

- Timeliness: It is very important that data is input to computer in time because outputs cannot be produced until certain inputs are available. Hence, a plan must be established regarding when different types of inputs will enter the system.
- Media: Various user input alternatives available in the market include display workstations, magnetic tapes, magnetic disks, key-boards, optical character recognition, pen-based computers and voice input etc. A suitable medium may be selected depending on the application to be computerised.
- Format: After the data contents and media requirements are determined, input formats are considered. While specifying the record formats, for instance, the type and length of each data field as well as any other special characteristics (number decimal places etc.) must be defined.
- Input volume: Input volume refers to the amount of data that has to be entered in the computer system at any one time. In some decision-support systems and many real-time transaction processing systems, input volume is light. In batch-oriented transaction processing systems, input volume could be heavy which involves thousands of records that are handled by a centralised data entry department using key-to-tape or key-to-disk systems.

6 a)

Systems Manual: The basic output of the system design is a description of the task to be performed, complete with layouts and flowcharts. This is called the job specifications manual or system manual. It contains:

- General description of the existing system.
- Flow of the existing system.
- Outputs of the existing system
- General description of the new system – its purposes & functions
- Flow of the operations of the new system
- Output Layouts.
- Output distribution - number of copies, routing and purpose in each department
- Input layouts describing inputs to the new system
- Responsibility for the source of each input document
- The overall logic of the internal flows
- The tape, disk or other
- Permanent record files to be maintained, and the items of information to be included in each file.
- A list of the programs to be written
- Timing estimates
- Type of controls, and the method in which it will be operated.
- Audit trail - a separate section of the systems specifications shows the audit trail for all financial information.
- Glossary of terms used.

b)

Advantages for using ready-made or pre-written application packages:

- Rapid implementation: Application packages are readily available to implement after they are purchased. In contrast, software developed in-house may take months or even years until it is ready for implementation.
- Low risk: Since the application package is available in the finished form, the organisation knows what it is going to get for the price it has paid. With in-house developed software, the long development time breeds uncertainty with regard to both the quality of the final product and its final cost.
- Quality: The firms engaged in application package developments have a lot of experience in their specialized application field and hence can provide better software. In contrast, in-house programs often have to work over a wide range of application areas; they may not be possessing expertise for undertaking proposed software development.
- Cost: Software vendors can leverage the cost of developing a product by selling the product to several other firms, thereby realising a lower cost from each application user. Thus, an application package generally costs less than an in-house developed package. Hence, application packages, sometimes, turn out to be cheaper compared to in-house developed software.
- Training: Vendors providing these software packages even impart training about how to use the software to its full potential.

PRIME ACADEMY

38th SESSION PROGRESS TEST - DIRECT TAX LAWS

No of Pages: 4 **Total Marks: 75**

Time Allowed: 2 Hrs

Question 1 is Compulsory. Answer any two from the rest.

Working notes should form part of the answer

Wherever necessary suitable assumptions may be made by the Candidates

1.

A. Fill in the blanks:

1. Manufacturing companies investing more than Rupees ________ in new plant and machinery during the period from 1.4.2013 to 31.3.2015 entitled to investment allowance @ 15%.
2. Basic Exemption Limit in case of resident individuals of the age 80 years or more is Rupees ____________ for Assessment Year 2014-15.
3. Rate of depreciation for Computers and Computer Software is allowed @ _______ % under the Income Tax Act, 1961.
4. A Gift of ₹ 80,0000/- received in Foreign Currency is _________ in case of Non Resident.
5. Capital Gains on transfer of quoted Zero Coupon Bonds after holding for a period of 24 Months, are taxable as _______ Term Capital Gains.

(5 x 1 = 5 Marks)

B. Identify the below as Taxable or Exempt based on the provisions of Income Tax Act, 1961:

1. Scholarship granted to meet the cost of education.
2. Income from sale of waste newspapers.
3. Income of Prasar Bharati (Broadcasting Corporation of India).
4. Daily allowance of Members of Parliament.
5. Proceeds from "Keyman Insurance Policy". (5 x 1 = 5 Marks)

C. State whether the statement is Correct or Incorrect :

1. Alternate Minimum Tax is applicable for Individuals and HUF.
2. Duty drawback received from Government under the Customs Act, is treated as Income under the Income Tax Act, 1961.
3. Stamp duty value of land and building to be taken as the full value of consideration in respect of transfer, even if the same are held by the transferor as stock-in-trade
4. Loss can be carried forward in case of filing of Income Tax Return beyond the due dates prescribed under Sec.139 of the Income Tax Act, 1961.
5. Cost of Improvement is allowed even in case of Intangible Assets.

(5 x 1 = 5 Marks)

D. Explain the following terms in brief with reference to Income Tax Act, 1961:

1. Agricultural Land u/s 2(14).
2. Business Connection u/s 9(1)(i).
3. Diversion of Income by overriding title.
4. Terminal Depreciation.
5. Inter Head Adjustment u/s 71. (5 x 2 = 10 Marks)

2.

A. Mr. Hari, a property dealer, sold a building in the course of his business to his friend Rajesh, who is a dealer in automobile spare parts, for ₹ 90 lakh on 1.1.2014, when the stamp duty value was ₹ 150 lakh. The agreement was, however, entered into on 1.7.2013 when the stamp duty value was ₹ 140 lakh. Mr. Hari had received a down payment of ₹ 15 lakh by cheque from Rajesh on the date of agreement. Discuss the tax implications in the hands of Hari and Rajesh, assuming that Mr. Hari has purchased the building for ₹ 75 lakh on 12th July, 2012.
Would your answer be different if Hari was a share broker instead of a property dealer?

(9 Marks)

B. Mr. X is a foreign citizen, not being a person of Indian Origin. Determine his residential status for AY 2014-15 on the assumption that during Financial years 1999-2000 to 2013-14, he was present in India as follows:

Financial Year	Days	Financial Year	Days
1999-2000	221	2007-08	96
2000-01	22	2008-09	286
2001-02	50	2009-10	100
2002-03	72	2010-11	182
2003-04	130	2011-12	85
2004-05	340	2012-13	280
2005-06	30	2013-14	86
2006-07	160		

(8 Marks)

C. The following are the particulars in respect of a scheduled bank incorporated in India –

S No.	**Particulars**	**₹ in Lakhs**
(i)	Provision for bad and doubtful debts under section 36(1)(viia) upto A.Y.2013-14	100
(ii)	Gross Total Income of A.Y.2014-15 [before deduction under section 36(1)(viia)]	800
(iii)	Aggregate average advances made by rural branches of the bank	300
(iv)	Bad debts written off (for the first time) in the books of account (in respect of urban advances only) during the previous year 2013-14	210

Compute the deduction allowable under section 36(1)(vii) for the A.Y.2014-15.

(4 Marks)

D. Briefly explain the rules for determining residential status of an Individual under Sec.6 of the Income Tax Act, 1961. (4 Marks)

3.

A. Alpha Ltd., a manufacturing company, which maintains accounts under mercantile system, has disclosed a net profit of ₹ 12.50 lacs for the year ending 31st March, 2014. You are required to compute the taxable income of the company for the Assessment year 2014-15, after considering the following information, duly explaining the reasons for each item of adjustment:

i. Advertisement expenditure includes the sum of ₹ 60,000 paid in cash to the sister concern of a director, the market value of which is ₹ 52,000.

ii. Legal charges include a sum of ₹ 45,000 paid to consultant for framing a scheme of amalgamation duly approved by the Central Government.

iii. Repairs of plant and machinery include ₹ 1.80 lacs towards replacement of worn out parts of machineries.

iv. A sum of ₹ 6,000 on account of liability foregone by a creditor has been taken to general reserve. The same was charged to the Revenue Account in the A.Y. 2011-12.

v. Sale proceeds of import entitlements amounting to ₹ 1 lac has been credited to Profit & Loss Account, which the company claims as capital receipt not chargeable to income-tax.

vi. Being also engaged in the biotechnology business, the company incurred the following expenditure on in-house research and development as approved by the prescribed authority:

(a) Research equipments purchased ₹ 1,50,000.

(b) Remuneration paid to scientists ₹ 50,000.

The total amount of ₹ 2,00,000 is debited to the Profit & Loss account.

(9 Marks)

B. B Ltd., a company engaged in the business of manufacture of sports equipments, furnishes the following particulars pertaining to P.Y. 2013-14 and P.Y.2014-15. Compute the depreciation allowable under section 32 as well as the investment allowance allowable under section 32AC for A.Y.2014-15 and A.Y.2015-16, while computing its income under the head "Profits and gains of business or profession". Also, compute the written down value of plant and machinery as on 1.4.2014 and 1.4.2015.

S No	Particulars	₹ in Crores
1	Written down value of plant and machinery (15% block) as on 01.04.2013	25
2	Sold plant and machinery on 20.5.2013 (15% block)	4
3	Purchase of second hand machinery (15% block) on 29.5.2013 for business purpose (the machinery was put to use immediately)	12
4	Purchased new computers (60% block) on 8.11.2013 for office	0.40
5	Acquired and installed new plant and machinery (15% block) on 31.7.2013 (₹ 50 crore) and on 31.10.2013 (₹ 40 crore)	90
6	New air conditioners purchased and installed in office premises on 30.6.2013	0.15
7	Acquired and installed new plant and machinery (15% block) on 2.4.2014	15

(9 Marks)

C. Explain the provisions with respect to "Income deemed to accrue or arise in India" u/s 9 of the Income Tax Act, 1961. Elucidate with examples. (7 Marks)

4.

A. Mr.X submits the following information relevant for the previous year ending on March 31, 2014.

Particulars	**₹**
Profits of Business A carried on in India	1,80,000
Loss of Business B carried on in India	(1,30,000)
Profits of Business C carried on in Canada(Income is earned and received in Canada and business is controlled in Canada)	1,40,000
Loss of Business D carried on in Canada(Though profits are not received in India, business is controlled from Delhi)	(1,70,000)
Unabsorbed Depreciation of Business D	1,52,000
Income from Property situated in India	1,12,000
Income from Property situated in Canada(received in Canada)	1,17,000

Determine the Net Income of Mr.X for the AY 2014-15 based on the assumption that he is a)resident and ordinarily resident in India, b) resident and not ordinarily resident in India, c)Non Resident in India. (10 Marks)

B. A piece of land owned by Mr. Bharti located on Yamuna Express highway was acquired by NHAI in the F.Y.2008-09, but the award ordered in F.Y. 2009-10 was paid in the F.Y. 2012-13. This land was purchased by him on 5.7.1980 for ₹ 25,000. The fair market value of the land as on 1.4.1981 was ₹ 22,500. Compensation paid was ₹ 38 lacs. The other piece of land located in Hyderabad purchased in February, 2004 for ₹ 62 lacs was also sold by him in February, 2014 for ₹ 88 lacs, but sale deed thereof could not be executed by 31.3.2014. The value for the purpose of stamp duty to be applied by the stamp valuation authority was ₹ 100 lacs. Compute the income chargeable to tax arising as a result of these transactions in the A.Y.2014-15.
The CIIs for the F.Y: 2003-04, 2008-09, 2009-10 and 2013-14 are 463, 582, 632 and 939 respectively. (8 Marks)

C. Briefly explain the taxability of Capital Gains on "Conversion of debentures into shares" u/s 49(2A) of the Income Tax Act, 1961. (4 Marks)

D. Explain the provisions with respect to "Disallowance of unpaid liability" u/s 43B of the Income Tax Act, 1961. (3 Marks)

PRIME ACADEMY
38TH SESSION PROGRESS TEST- DIRECT TAX LAWS
SUGGESTED ANSWERS
PART- A

1) A)
   1. ₹ 100 Crores
   2. ₹ 500,000/-
   3. 60%.
   4. Taxable.
   5. Short Term Capital Gains.

   B)
   1. Exempt
   2. Taxable
   3. Exempt
   4. Exempt
   5. Taxable

   C)
   1. Correct.
   2. Correct.
   3. Correct.
   4. Incorrect.
   5. Correct.

   D) 1. Agricultural Land u/s 2(14).

   (a) In any area which is comprised within the jurisdiction of a municipality (whether known as a municipality, municipal corporation, notified area committee, town area committee, town committee, or by any other name) or a cantonment board and which has a population of not less than ten thousand according to the last preceding census of which the relevant figures have been published before the first day of the previous year or

   (b) In any area within the distance, measured aerially,—

   (i) not being more than two kilometers, from the local limits of any municipality or cantonment board referred to in item (a) and which has a population of more than ten thousand but not exceeding one lakh; or

   (ii) not being more than six kilometers, from the local limits of any municipality or cantonment board referred to in item (a) and which has a population of more than one lakh but not exceeding ten lakh; or

   (iiiI) not being more than eight kilometers, from the local limits of any municipality or cantonment board referred to in item (a) and which has a population of more than ten lakh.

   2. Business Connection u/s 9(1)(i)

   As per section 9(1)(i) of the Act where any income arises to a non resident though a business connection in India, then such income is deemed to accrue or arises in India and hence taxable in India. However, the term business connection has been defined in the Act in an inclusive manner to include activities carried on through dependent agency. There is no definitive meaning of the term business connection and so steering needs to be drawn from various judicial precedents which have probed the scope and meaning of the term business connection.

The principle engrossing from judicial precedent on the term "business connection" can be summarized as under:

- Business connection means something more than business;
- There should be some connection between business carried on by non-resident which earn profit and some activity in India;
- There should be a real and intimate relation between the trading activity carried on outside India and trading activity in India; and
- There should be an element of continuity between the business of non-resident and activity in India.

3. Diversion of Income by overriding title

   In determining whether there has been diversion of income by overriding title, it is the nature of the obligation which is the decisive fact. There is a difference between an amount which a person is obliged to apply out of this income and an amount which by the nature of the obligation cannot be said to be a part of the income of the assessee. Where by an obligation, income is diverted before it reached the assessee, it is deductible; but where the income is required to be applied to discharge an obligation after such income reaches the assessee, the same consequence, in law, does not follow. It is the first kind of payment which can truly be excused and not the second. The second payment is merely an obligation to pay another a portion of one's income, which has been received and is since applied. The first is a case in which the income never reaches the assessee, who even if he were to collect it, does so, not as part of his income, but for and on behalf of the person to whom it is payable."

4. Terminal Depreciation

   Where an asset on which depreciation has been claimed u/s 32(1)(i) and which is sold, destroyed or discarded; and If Sales Consideration is less than the Actual cost minus Depreciation allowed; then, difference between above two factors shall be allowed as terminal depreciation in the previous year in which it is sold; destroyed or discarded.

5. Inter Head Adjustment u/s 71.

   As explained above, any loss from one source of income is firstly set off against any gain from another source within the same head. Any remaining loss can then be set off against Income from any other Head. This is known as Inter-Head adjustment. However, there are exceptions to this rule also as discussed below. Following are the exceptions to inter-head adjustment

   a. No loss of whatsoever nature can be set off against winnings from lotteries, crossword puzzles, card games etc.
   b. Loss from a speculation business;
   c. Loss from the activity of owning and maintaining race horses;
   d. Loss from a source which is exempt.
   e. Long-term capital loss- only from LTCC

2)

A. **Case 1: Tax implications if Mr. Hari is a property dealer**

In the hands of Mr. Hari	In the hands of Mr. Rajesh
In the hands of Hari, the provisions of section 43CA would be attracted, since the building represents his stock-in-trade and he has transferred the same for a consideration less than the stamp duty value on the date of agreement. Therefore, ₹ 65 lakh, being the difference between the stamp duty value on the date of agreement (i.e., ₹ 140 lakh) and the purchase price (i.e., ₹ 75 lakh), would be chargeable as business income in the hands of Mr. Hari.	Since Mr. Rajesh is a dealer in automobile spare parts, the building purchased would be a capital asset in his hands. The provisions of section 56(2)(vii) would be attracted in the hands of Mr. Rajesh who has received immovable property, being a capital asset, for inadequate consideration. Therefore,₹50 lakh, being the difference between the stamp duty value of the property (i.e., ₹ 140 lakh) and the actual consideration (i.e., ₹90 lakh) would be taxable under section 56(2)(vii) in the hands of Mr. Rajesh.

Case 2: Tax implications if Mr. Hari is a stock broker

In the hands of Mr. Hari	In the hands of Mr. Rajesh
In case Mr. Hari is a stock broker and not a property dealer, the building would represent his capital asset and not stock-in-trade. In such a case, the provisions of section 50C would be attracted in the hands of Mr. Hari and ₹ 75 lakh, being the difference between the stamp duty value on the date of registration (i.e., ₹ 150 lakh) and the purchase price (i.e., ₹ 75 lakh) would be chargeable as short term capital gains. It may be noted that under section 50C, there is no option to adopt the stamp duty value on the date of agreement, even if the date of agreement is different from the date of registration and part of the consideration has been received on or before the date of agreement otherwise than by way of cash.	There would be no difference in the taxability in the hands of Mr. Rajesh, whether Mr. Hari is a property dealer or a stock broker. Therefore, the provisions of section 56(2)(vii) would be attracted in the hands of Mr. Rajesh who has received immovable property, being a capital asset,for inadequate consideration. Therefore, ₹ 50 lakh, being the difference between the stamp duty value of the property (i.e., ₹140 lakh) and the actual consideration (i.e., ₹90 lakh) would be taxable under section 56(2)(vii) in the hands of Mr. Rajesh.

B. For the Assessment Year 2014-15, financial year 2013-14 is the previous year. During 2013-14, X is in India for a period of 86 days and during four years preceding the previous year 2012-13, he is in India for 647 days. Thus he satisfies one of the two basic conditions laid down by Section 6(1) and consequently he becomes resident in India. A resident individual may either be an ordinarily resident or not ordinarily resident. To determine whether X is ordinarily resident or not ordinarily resident, one has to test the two additional conditions as laid down by Section 6(6)(a) as below:

Year	Presence in India	Status	Condition (a) or (b)
2012-13	280	Resident	(a) or (b)
2011-12	85	Resident	(b)
2010-11	182	Resident	(a) or (b)
2009-10	100	Resident	(b)
2008-09	286	Resident	(a) or (b)
2007-08	96	Resident	(b)
2006-07	160	Resident	(b)
2005-06	30	Non Resident	None
2004-05	340	Resident	(a)
2003-04	130	Resident	(b)
2002-03	72	Not necessary to determine	
2001-02	50		
2000-01	22		
1999-00	221		

X satisfies one of the two basic conditions and the two additional conditions. He is therefore Resident and Ordinarily Resident.

C.

Deduction allowable under section 36(1)(vii) for the A.Y.2014-15

Particulars	**₹ in Lakhs**	**₹ in Lakhs**
Bad debts written off (for the first time) in the books of account		210
Less: Credit balance in the "Provision for bad and doubtful debts" under section 36(1)(viia) as on 31.3.2014: (i) Provision for bad and doubtful debts under section 36(1)(viia) Up to A.Y.2013-14 (ii) Current year provision for bad and doubtful debts under section 36(1)(viia) [7.5% of ₹ 800 lakhs + 10% of ₹ 300 lakhs]	100 90	190
Deduction under section 36(1)(vii) in respect of bad debts written off for A.Y.2014-15		**20**

D. For determining the Residential Status of an Individual one has to pass the litmus test of two broad situations, First is the testing of two Basic Conditions u/s 6(1) , and Second is the testing of other two Additional Conditions U/s 6(6)

E.

Basic Condition (a)	He/She is in India in the previous year for a period of 182 days or more.
Basic Condition (b)	He/She is in India for a period of 60 days or more during the previous year and 365 days or more during 4 years immediately preceding the previous year.

The above period of 60 days gets extended to 182 days in the following three situations:

1) If you being an Indian Citizen leave India during the previous year for the purpose of employment outside India; or,
2) If you being an Indian Citizen leave India during the previous year as a member of the crew member of an Indian Ship.
3) If you being an Indian Citizen or a Person of Indian Origin come to visit India during the previous year.

ADDITIONAL CONDITIONS:

Additional Condition (a)	He has been "resident" in India in at least 2 out of 10 previous years immediately preceding the relevant previous year.
Additional Condition (b)	He has been in India for a period of 730 days or more during 7 years immediately preceding the relevant previous year.

- Here you must note that unlike testing of the two basic conditions as mentioned above here the Individual has to satisfy both the conditions simultaneously to qualify him/ herself as a 'Resident and Ordinarily Resident' (abbreviated as ROR)
- However if an Individual is able to satisfy either none or only one of the two additional conditions specified above he qualifies himself as a 'Resident but not Ordinarily Resident' (abbreviated as RNOR).

3)

A. Computation of taxable income of Alpha Ltd. for the A.Y. 2014-15

Particulars	₹
Net profit as per profit and loss account	12,50,000
<u>Add: Items debited to profit and loss A/c but not deductible</u>	
1. Payment of advertisement expenditure of ₹ 60,000	
(i) ₹ 8,000, being the excess payment to a relative disallowed Under Section 40A(2)	8,000
(ii) As the payment is made in cash and since the remaining amount of₹ 52,000 exceeds ₹ 20,000, 100% shall be disallowed under section 40A(3)	52,000

2. Legal charges for framing amalgamation scheme (deductible under section 35DD in five years). 1/5th of₹ 45,000 i.e. ₹ 9,000 to be allowed in the current year. Balance₹36,000 (₹ 45,000 -₹ 9,000) is to be added back.(See Note below)	36,000
3. Under section 31, expenditure relatable to current repairs regarding plant, machinery or furniture is allowed as deduction. The test to determine whether replacement of parts of machinery amounts to repair or renewal is whether the replacement is one which is in substance replacement of defective parts or replacement of the entire machinery or substantial part of the entire machinery - CIT v. Darbhanga Sugar Co. Ltd. [1956] 29 ITR 21 (Pat). Here expenditure on repairs does not bring in any new asset into existence. Such replacement can only be considered as current repairs. Hence, no adjustment is required.	6,000
Add: Items chargeable as business income but not credited to profit and loss A/c	
4. Liability foregone by creditor [taxable under section 41(1)]	
5. Sale proceeds of import entitlements. The sale of the rights gives rise to profits or gains taxable under section 28(iiia). As the amount has already been credited to Profit and Loss Account, no further adjustment is necessary.	
Less: Amount not debited to profit and loss account but allowable as deduction	
6. Expenditure on in-house research and development is entitled to a weighted deduction of 200% of the expenditure (both capital and revenue) so incurred under section 35(2AB)(1) = ` 2 lacs x 200% = ` 4 lacs. Expenditure of ` 2,00,000 has already been debited to Profit & Loss Account, therefore only additional deduction of ` 2 lacs further to be allowed 2,00,000	2,00,000
TAXABLE INCOME	**11,52,000**

Note: As per the provisions of section 35DD, any expenditure incurred wholly and exclusively for the purpose of amalgamation, would be allowed as a deduction in 5 successive years (1/5th each year) commencing from the year in which the amalgamation takes place. The problem has been worked out on the assumption that the amalgamation has taken place during the previous year itself.

(9 Marks)

B. Computation of depreciation allowance under section 32 for the A.Y. 2014-15

Particulars		Plant & Machinery (15%)	Plant & Machinery (60%)
		(₹ in Crores)	
WDV as on 01.04.2013		25	
Add: Plant and Machinery acquired during the year			
- Second hand machinery	12.00		
- New plant and machinery	90.00		
- Air conditioner installed in office	0.15	102.15	
Computers acquired during the year		-	0.40

	127.15	0.40
Less: Asset sold during the year	4.00	Nil
Written down value before charging depreciation	123.15	0.40
Less: Depreciation for the P.Y.2013-14 (See Note 1 below)	29.47	0.12
WDV as on 1.4.2014	93.68	0.28
Note 1 : Computation of depreciation for the P.Y.2013-14		
Normal depreciation		
Depreciation@30% on computers put to use for less than 180 days (50% of 60% × ₹ 0.40 crore)	-	0.12
Depreciation on plant and machinery (15% block) (40 × 7.5%) + [(123.15-40) × 15%]	15.47	-
Additional depreciation		
- New plant and machinery installed on 31.7.2013 (₹ 50 crore × 20%) = 10	14	Nil
- on 31.10.2013 (₹ 40 crore × 10%) = 4	**29.47**	**0.12**
Total depreciation		

Note – For the A.Y.2014-15, the company would not be entitled for investment allowance under section 32AC since the investment in new plant and machinery acquired and installed during the year is only ₹90 crores (i.e., less than ₹ 100 crores). Investment in second hand plant and machinery and air-conditioners and computers installed in office would not be eligible for investment allowance under section 32AC or additional depreciation under section 32(1)(iia).

Computation of depreciation allowance under section 32 for the A.Y. 2015-16

Particulars	Plant & Machinery (15%)	Plant & Machinery (60%)
	(₹ in Crores)	
WDV as on 1.4.2014	93.68	0.28
Add: Plant and Machinery acquired during the year	15.00	-
	108.68	0.28
Less: Asset sold during the year	Nil	Nil
Written down value (before charging depreciation)	108.68	0.28
Less: Depreciation for the P.Y.2014-15 @15% and 60%, respectively	16.30	0.17
Additional depreciation@20% on 15 crore	3.00	-
WDV as on 1.4.2015	**89.38**	**0.11**

Computation of investment allowance under section 32AC for the A.Y.2015-16

Particulars	**₹ in Crores**
New plant and machinery acquired and installed during the P.Y.2013-14	90
New plant and machinery acquired and installed during the P.Y.2014-15	15
Aggregate investment in new plant and machinery during 1.4.2013 to 31.3.2015	105
Investment allowance@15% of ₹ 105 Crores	15.75
Less: Deduction allowed in respect investment allowance during the A.Y.2014-15	Nil
	15.75

Deduction under section 32AC for the A.Y.2015-16	

Note - The company would be eligible for investment allowance under section 32AC in the P.Y.2014-15, since the aggregate investment in new plant and machinery from 1.4.2013 to 31.3.2015 has exceeded ₹ 100 crore.

C. Section 9(1)(i) provides that income is deemed to accrue or arise in India if it accrues, 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 situate in India

Explanation to section 9(1)(i) provides for following exemptions.

- In the case of business of which all the operations are not carried out in India, only such part of the income as is reasonably attributable to the operations carried out in India would be the income deemed to accrue or arise in India.
- No income shall be taxable in India if the operations of the non-resident is confined to the purchase of goods in India for the purpose of export

In case of non-resident engaged in the business of running a news agency or of publishing newspapers, magazines or journals, no income shall be taxable in India if the activities confined to the collection of news and views in India for transmission out of India

- In case of non-resident no income shall be taxable in India if the operations are confined to the shooting of any cinematograph film in India.

The deeming provisions of section 9 are careful to describe the connection or the nexus between such income and India. The nexus is either

- business connection in India or
- the property in India or
- asset or source in India or
- capital asset in India

4)

A.

Particulars	**Resident & Ordinarily Resident** ₹	**Resident but not ordinarily resident** ₹	**Non-Resident** ₹
Business Income			
Business A	1,80,000	1,80,000	1,80,000
Business B	-1,30,000	-1,30,000	-1,30,000
Business C (Income is not taxable)	1,40,000	Nil	Nil
Business D (Business Income earned and received out of India is not taxable in the hands of non-resident. Loss arising from such business is therefore not deductible)	-1,70,000	-1,70,000	Nil
Unabsorbed Depreciation of business D	-1,52,000	-1,52,000	Nil

Business Income/loss	**-1,32,000**	**-2,72,000**	**-50,000**
Income from Property situated in India	1,12,000	1,12,000	1,12,000
Income from Property situated in Canada(received in Canada)	1,17,000	Nil	Nil
Gross Total Income	97,000	-1,60,000	1,62,000
Less: Deductions u/s 80C to 80U	Nil	Nil	Nil
Net Income / Loss	97,000	-1,60,000	1,62,000

B. A piece of land owned by Mr. Bharti located on Yamuna Express highway was acquired by NHAI in the F.Y.2008-09, but the award ordered in F.Y. 2009-10 was paid in the F.Y. 2012-13. This land was purchased by him on 5.7.1980 for ₹ 25,000. The fair market value of the land as on 1.4.1981 was ₹ 22,500. Compensation paid was₹ 38 lacs. The other piece of land located in Hyderabad purchased in February, 2004 for ₹ 62 lacs was also sold by him in February, 2014 for ₹ 88 lacs, but sale deed thereof could not be executed by 31.3.2014. The value for the purpose of stamp duty to be applied by the stamp valuation authority was ₹ 100 lacs. Compute the income chargeable to tax arising as a result of these transactions in the A.Y.2014-15.
The CIIs for the F.Y: 2003-04, 2008-09, 2009-10 and 2013-14 are 463, 582, 632 and 939 respectively.

Computation of taxable income of Mr. Bharti for A.Y.2013-14

Particulars	₹
Capital Gains	
(A) Long-term capital gain derived from transfer of land on Yamuna Express highway acquired by NHAI in F.Y. 2008-09 for which award was paid in F.Y. 2012-13 is chargeable to tax in A.Y.2013-14 [See Note (i) below]	
Sale consideration i.e. compensation paid	38,00,000
Less: Indexed cost of acquisition [See Note (ii) below] (25,000 x 582/100)	1,45,500
	36,54,500
(B) Sale of land at Hyderabad in February 2014 [See Note (iii) below]	
Full value of consideration as per section 50C [See Note (iv) below]	1,00,00,000
Less: Indexed cost of acquisition (₹62,00,000 × 939)/463 : 12574082	1,25,74,082
	(25,74,082)

Total income chargeable to tax arising as a result of these transactions in the A.Y.2014-15 is equal to ₹ 10,80,418 (i.e. ₹ 36,54,500 - ₹ 25,74,082). Long term capital loss can be set-off from the long term capital gain.

Notes:

(i) The capital gains arising on compulsory acquisition shall be charged to tax in the year in which the compensation is first received as per section 45(5)(a). However, the indexation benefit would be available only up to the year in which the property was compulsorily acquired i.e. F.Y. 2008-09.

(ii) The option of fair market value as on 1.4.81 is not exercised by the assessee since the fair market value is lower than the cost.

(iii) The execution of sale deed is not compulsory for the purpose of charge of capital gain because the transfer of right enabling enjoyment of immovable property gives rise to charge of capital gains as held by the Kerala High Court in the case of CIT v. C.F. Thomas (2006) 284 ITR 557.

(iv) As per section 50C, the value applied by the stamp valuation authority is deemed to be the full value of consideration received or accruing as a result of such transfer, since such value is higher than the sale consideration of ₹ 88 lacs. 939 is the cost inflation index of F.Y.2013-14 i.e. the year in which the property at Hyderabad was sold.

C. When the debentures are converted in to shares and if later, the shares are sold, THE COST of such shares u/s 49(2A) shall be the cost incurred to acquire that part of Debentures which are converted into the shares thus sold., but the period of holding of Debenture is not permitted to be included in the period of holding of such shares for computing the capital gain. In other words since it is the share which is sold, the period of holding will be the period from the date of allotment of shares. Also, indexation benefit for shares (If Long term) can be taken from the date of conversion into shares and not from the date of holding of debentures. It should be remembered that from A.Y. 1998-99,no indexation benefit in respect of transfer of Debentures/Bonds (Except Capital Indexed Govt Bonds) is available.

D. In computation of income under the head **Profits and gains of business or profession** (PGBP), some of the expenses are allowed under Income Tax Act 1961 and can be claimed by the assessee only in the year in which the payment is actually made.

As per Section 43B

a. any sum payable by the assessee by way of tax, duty, cess or fee, (by whatever name called, under any law for the time being in force);
b. any sum payable by the assessee as an employer by way of contribution to any provident fund or superannuation fund or gratuity fund or any other fund for the welfare of employees;
c. any sum payable as bonus or commission to employee for services rendered;
d. any sum payable by the assessee as interest on any loan or borrowing from any public financial institution or a State financial corporation or a State industrial investment corporation, in accordance with the terms and conditions of the agreement governing such loan or borrowing;
e. any sum payable by the assessee as interest on any loan or advances from a scheduled bank in accordance with the terms and conditions of the agreement governing such loan or advances;
f. any sum payable by the assessee as an employer in lieu of any leave at the credit of his employee shall be allowed as deduction only in the previous year in which such sum is actually paid. This is irrespective of the previous year in which the liability to pay such sum was incurred by the assessee.

PRIME ACADEMY

38th SESSION PROGRESS TEST

INDIRECT TAXES

No. of pages -4 **Total Marks – 75**

Part - A **Time Allowed-2 Hrs**

Answer all Questions

Working notes should form part of the answer.

Wherever necessary, suitable assumptions may be made by the students

1. 'M Agro Handlers' furnishes the following details with respect to the activities undertaken by undertaken by them in the month of Dec 2013

S.No	Particulars	Amount (₹)
(i)	Supply of farm labour	58,000
(ii)	Warehousing of biscuits	1,65,000
(iii)	Sale of rice on commission basis	68,000
(iv)	Training of farmers on use of new pesticides and fertilizers developed through scientific research	10,000
(v)	Renting of vacant land to a stud farm	1,31,500
(vi)	Testing undertaken for soil of a farm land	1,21,500
(vii)	Leasing of vacant land to a poultry farm	83,500

Compute the service tax liability of 'M Agro Handlers' for the month of Dec, 2013. Assume that the point of taxation in respect of all the activities mentioned above falls in the month of Dec, 2013 itself.

'M Agro Handlers' has paid service tax of INR 6,18,000 during the Financial Year 2012-13.

(5 Marks)

2. Answer the following with reference to the applicability of service tax as per the amended provisions of service tax
   a) Transport facility provided by a School to its students through a fleet of busesand cabs owned by the School.
   b) Transportation of petroleum and petroleum products and household effects byrailways.
   c) Service provided in relation to repair or maintenance of aircraft owned by aState Government.
   d) Services of a NGO registered under section 12AA of the Income tax Act, 1961working for the rehabilitation of disabled. The aggregate value of taxableservices of the NGO is INR 20 lakh.
   e) Exhibiting movies on television channels. (5 Marks)

3. Explain the below question, with the help of a recently decided case law
   a) Whether expenditure like travel, hotel stay, transportation and the like incurred by service provider in course of providing taxable service should be treated as consideration for taxable service and included in value for charging service tax? (5 Marks)

   (OR)

   b) Is the service tax and excise liability mutually exclusive? (5 Marks)

4.

(i) Bansal Ltd. is located in India and holding 60% shares of Aggarwal Ltd., a U.K.based company. The latter company [Aggarwal Ltd.] provides public relation services to former company [Bansal Ltd.] The other relevant details are given below

Agreed Consideration	£ 2,00,000/-
Date on which services are provided by Aggarwal Ltd.	16.07.2013
Date on which invoice is sent by Aggarwal Ltd.	19.07.2013
Date of debit in the books of account of Bansal Ltd.	31.07.2013
Date on which payment is made by Bansal Ltd.	23.10.2013

Determine Point of Taxation for Bansal Ltd. (3 Marks)

(ii) Determine the place of provision of service in accordance with the Place of Provision of Services Rules, 2012 in the following cases:-

a) Samuel, a well-known singer from Singapore, organises a Rock Concert in Delhi and Mumbai. It undertook the event management services from Beta Services Ltd.

b) Laxmi& Co., an Indian firm, provides 'technical inspection and certification service' for a newly developed product of an overseas firm (for a newly launched motorbike which has to meet emission standards in different States or countries). The testing is carried out in Gujarat (20%), Kerala (25%), and Colombo (55%) (2 Marks)

5. What is the objective of bringing certain services under "Declared Services"? Mention any three services which fall within the scope of "Declared Services" (5 Marks)

Part – B (50 Marks)

Answer all Questions

Working notes should form part of the answer

Wherever necessary, suitable assumptions may be made by the students

1.

a) Determine the assessable value under the subject transaction under section 4 of the Central Excise Act, 1944? Give reasons with suitable assumptions where necessary.

		₹
	Contracted sale price for delivery at buyer's premises	10,00,000
	The contracted sale price includes the following elements of cost:	
(i)	Cost of drawings and designs	6,000
(ii)	Cost of primary packing	4,000
(iii)	Cost of packing at buyer's request for safety during transport	9,000
(iv)	Excise duty	1,11,200
(v)	VAT (Sales tax)	37,000
(vi)	Octroi	9,500
(vii)	Freight and insurance charges paid from factory to 'place of removal'	27,000
(viii)	Actual freight and insurance from 'place of removal' to buyer's Premises	42,300

b) Sahu& Co., a SSI unit, manufactures different products and the value of clearances for the financial year 2013-14 is given below:

(₹in lakhs)

S. No	Product	AB	SA	AS
(i)	Clearance for home consumption	55	40	60
(ii)	Captive consumption in the manufacture of excisable goods	120	90	70
(iii)	Export to U.S.A.	80	70	Nil
(iv)	Export to Nepal	50	40	39
(v)	Job work done under Notification No. 214/86-C.E.	65	40	70
(vi)	Goods manufactured in rural area with brand name of	45	35	35

The unit seeks your advice as to whether they are eligible for SSI exemption for the year 2014-15. Explain the basis for your conclusions. (2*5=10 Marks)

2. a)

Ms X Restaurants Ltd ('X India') manufactures and served 'soft serves' dispensed through vending machines at its restaurants. The Department raised a demand for the excise duty on the fast-food restaurant chain. It contended that 'soft serve' was classifiable under Heading 21.05,Sub-Heading 2105.00-"ice cream and other edible ice, whether or not containing cocoa" and thus, would attract excise duty @ 16% plus an additional duty (applicable at the relevant time).

However, X India opposed the classification sought by the Department and claimed that the 'soft serve' was classifiable under Heading 04.04 as "other dairy produce" chargeable to nil rate of duty. Hence, it was not required to pay any duty.
The Department has claimed that although "ice-cream" had not been defined under Heading 21.05 or in any of the chapter notes of Chapter 21, 'soft serve' was known as "ice-cream" in common parlance. Therefore, soft serve' must be classified in the category of "ice-cream" under Heading 21.05 of the Tariff Act.

On the other hand, the X India contended that 'soft serve' must be classified under Heading 04.04 as "other dairy produce" and not under Heading 21.05.
Explain with the help of a recently decided case law, whether contention of X India is valid.

b) Cars Ltd (CL) was the manufacturer of motor cars. They were selling CL-5 model cars below cost and were making losses in whole sale trade. The purpose was penetration of market and competing with other manufacturers of similar goods. The prices were not based on manufacturing cost and profit. The cost of production of the cars was much more than their wholesale price, but they were being sold at loss for a consideration. This was happening over the period of five years.
The Department disputed that as the extra commercial consideration was involved in this case, an additional consideration should be added to the price for the purpose of duty.
Explain with decided case whether selling price could be accepted as transaction value.
(2*5=10 Marks)

3.

i) Bring out the conditions under which MRP valuation shall apply under Central Excise Act, 1944. (4 Marks)

ii) Examine the validity of the following statements:

a) In case of services relating to life insurance, provider of output service is obligated to pay every month an amount equal to 20% of the CENVAT credit availed on inputs and input services in that month.

b) An assessee sold certain goods to PQR Ltd. for ₹ 20,000 (excluding excise duty and other taxes) on 09.09.2013. The buyer, PQR Ltd., is a related person as defined under section 4(3)(b) of the Central Excise Act, 1944. It did not sell the goods, but used it as intermediary product. The cost of production of the said goods determined as per CAS-4 was ₹ 16,000. Determine the assessable value in the given case. What will be the assessable value, if in the aforesaid case, PQR Ltd. is not related to the assessee? (2*2=4 Marks)

(iii) Under what circumstances can a Central Excise Officer make best judgement assessment under service tax law? (2 Marks)

4. a) Explain the below questions with the help of a recently decided case law “Can a product short shelf-life of 2 to 3 days be considered marketable”

b) Differentiate between "non-excisable goods" and "non-dutiable goods".

(2*5=10 Marks)

5 a)

i) Explain briefly the significance of “trade parlance test” with respect to classification of excisable goods under the Central Excise Act, 1944. (4 Marks)

ii) When a person shall be deemed to be a related person for the purpose of valuation under the Central Excise Act? (4 Marks)

iii) The maxim "Latter the Better" applies in classifying the excisable goods. Discuss.

(2 Marks)

(OR)

5 b)

i) Differentiate between compounded levy scheme and duty based on annual production capacity under central excise. (5 Marks)

ii) Explain briefly with reference to the provisions of the Central Excise Act the term “Deemed Manufacture”. (5 Marks)

PRIME ACADEMY
38TH SESSION PROGRESS TEST- INDIRECT TAX
SUGGESTED ANSWERS
Part - A

1.

Computation of Service Tax payable by M Agro Handlers for Dec 2013

S. No.	Particulars	Amount (₹)
(i)	Supply of farm labour [Note 1]	-
(ii)	Warehousing of biscuits [Note 3]	1,65,000
(iii)	Sale of rice on commission basis [Note 1]	-
(iv)	Training of farmers on use of new pesticides and fertilizers developed through scientific research [Note 1]	-
(v)	Renting of vacant land to a stud farm [Note 2]	
(vi)	Testing undertaken for soil of a farm land [Note 1]	1,31,500
(vii)	Leasing of vacant land to a poultry farm [Note 2]	-
	Total	2,96,500
	Service Tax @12.36% (Rounded Off)	36,647

Notes:

(1) Clause (d) of negative list of services [section 66D] covers 'services relating toagriculture or agricultural produce by way of inter alia –
   (i) supply of farm labour
   (ii) services provided by a commission agent for sale or purchase of agriculturalproduce
   (iii) agricultural extension services. Agriculture extension means application of scientificresearch and knowledge to agricultural practices through farmer education ortraining.
   (iv) agricultural operations directly related to production of any agricultural produceincluding testing.

(2) Services relating to agriculture or agricultural produce by way of renting or leasing of vacant land are covered under clause (d) of section 66D. Agriculture means the cultivation of plants and rearing of all life-forms of animals, except the rearing of horses, for food, fibre, fuel, raw material or other similar products. Thus, leasing of vacant land to a poultry farm will be included in the negative list but renting of vacant land to a stud farm will be outside the purview of negative list.

(3) Loading, unloading, packing, storage or warehousing of agricultural produce is covered under clause (d) of Section 66D. However, agricultural produce means any produce of agriculture on which either no further processing is done or such processing is done as is usually done by a cultivator or producer which does not alter its essential characteristics but makes it marketable for primary market. Thus, warehousing of biscuit will be taxable as biscuit is not an agricultural produce.

(4) As M Agro Handler has paid service tax of ₹ 6,18,000 during the FY 2012-13, it is not eligible to small service providers exemption provided under Notification No. 33/2012 ST dated 20.06.2012 in the FY 2013-14.

2.

(i) Taxable. Transport facility provided by a School to its students is an auxiliary educational service. With effect from 01.04.2013, the exemption provided to the auxiliary educational services provided by an educational institution has been withdrawn [Mega Exemption Notification No. 25/2012 ST dated 20.06.2012 amended].

(ii) Taxable. With effect from 01.04.2013, exemption granted to transportation of petroleum and petroleum products and household effects by railways has been withdrawn [Mega Exemption Notification No. 25/2012 ST dated 20.06.2012 amended].

(iii) Taxable. With effect from 01.04.2013, the exemption provided in relation to repair or maintenance of aircraft owned by Government (Government includes State Government) has been withdrawn [Mega Exemption Notification No. 25/2012 ST dated 20.06.2012 amended].

(iv) Taxable. With effect from 01.04.2013, the exemption available to entities registered under section 12AA of the Income tax Act, 1961 providing services for advancement of "any other object of general public utility" up to ₹ 25 lakh has been withdrawn [Mega Exemption Notification No. 25/2012 ST dated 20.06.2012 amended].

(v) Taxable. With effect from 01.04.2013, the benefit of exemption in relation to copyrights for cinematograph films has been restricted only to films exhibited in a cinema hall or theatre. Therefore, exhibition of cinematograph films in a place other than cinema hall or theatre, will be taxable [Mega Exemption Notification No. 25/2012 ST dated 20.06.2012 amended].

3.

(a) The above question came up for consideration before the Delhi High Court in case of Intercontinental Consultants & Technocrats Pvt. Ltd. v. Union of India 2013 (29) S.T.R. 9 (Del.). The High Court noted that as per Rule 5(1) of the Service Tax (Determination of Value) Rules, 2006 (hereinafter referred to as Rules),expenditure/costs, such as travel, hotel stay, transportation, etc. incurred by service provider in course of providing taxable service has to be treated as consideration for taxable service and included in value for charging service tax. The High Court observed that since section 67(1) of Finance Act, 1994 is subject to provisions of Chapter V - which includes section 66 (now section 66B) – the value of taxable services has to be in consonance with section 66 which levies tax only on taxable service. Thus, there is an inbuilt mechanism to ensure that only taxable service are evaluated under section 67 which provides that value of taxable service is the gross amount charged by service provider 'for such service'. The High Court, therefore, opined that it is only the consideration for the taxable service which is chargeable to tax under the relevant Sections. However, rule 5(1) goes far beyond the charging provisions as it includes the expenditure and costs - which are incurred by the service provider "in the course of providing taxable service" - in the value of the taxable service.

The High Court elaborated that power to make rules could not exceed or go beyond the section which provides for charge or collection of service tax. The High Court clarified that even though section 94 prescribes to lay every rule framed by Central Government before each House of Parliament, which have power to modify them; the same cannot add any greater force to the Rules than what they ordinarily have as species of sub ordinate legislation.

The High Court further observed that rule 5(1) may also result in double taxation, if expenses like air travel tickets, had already been subjected to service tax. The High Court was of the view that double taxation can be imposed only when it is clearly provided for and intended. It can never be enforced by implication.
The High Court, therefore, held that rule 5(1) of the Rules runs counter and is repugnant to sections 66 and 67 of the Act and to that extent it is ultra vires the Finance Act, 1994.

(OR)

(b) The High Court in the case of Commissioner of Service Tax v. Lincoln Helios (India) Ltd. 2011 (23) S.T.R. 112 (Kar) held that the excise duty is levied on the aspect of manufacture and service tax is levied on the aspect of services rendered.
Hence, it would not amount to payment of tax twice and the assessee is liable to pay service tax on the value of services.

4

(i) By virtue of its aforementioned shares in Aggarwal Ltd., Bansal Ltd. Becomes the holding company of Aggarwal Ltd as per section 4 of Companies Act,1956. Resultantly, both Bansal Ltd. and Aggarwal Ltd. will fall within the ambit of the term "associated enterprises" as per section 92A of Income Tax Act, 1961. As a result, second proviso to Rule 7 of Point of Taxation Rules, 2011 becomes applicable in the present case. Thus, Point of Taxation will be determined in the following manner:
Earlier of the following two dates:
Date of debit in the books of account of person receiving the service [which is Bansal Ltd. in the present case] 31.07.2013
Date of making the payment [by Bansal Ltd. in the present case] 23.10.2013
Thus, Point of Taxation will be 31.07.2013.

(ii)

(a) As per rule 6 of the Place of Provision of Services Rules, 2012, place of provision of services provided by way of admission to, or organization of, a cultural, artistic, sporting, scientific, educational, or entertainment event, or a celebration, conference, fair, exhibition, or similar events, and of services ancillary to such admission, shall be the place where the event is actually held. Since in the given case, event is held in India, place of provision of services is India.

(b) As per rule 7 of the Place of Provision of Services Rules, 2012, where any service referred to in rules 4, 5, or 6 is provided at more than one location, including a location in the taxable territory, its place of provision shall be the location in the taxable territory where the greatest proportion of the service is provided. In the given case, notwithstanding the fact that the greatest proportion of service is outside the taxable territory, the place of provision will be the place in the taxable territory where the greatest proportion of service is provided, which in this case is Kerala.

5. The objective of bringing certain services within the purview of 'declared service' is to remove any ambiguity for the purpose of uniform application of law all over the country. Following services have been brought within the ambit of 'declared service' under section 66E of the Finance Act, 1994:

(i) Renting of immovable property
(ii) Construction of a complex, building, civil structure or a part thereof, including a complex or building intended for sale to a buyer, wholly or partly, except where the entire consideration is received after issuance of completion certificate by the competent authority
(iii) Temporary transfer or permitting the use or enjoyment of any intellectual property right
(iv) Development, design, programming, customization, adaptation, up gradation, enhancement, implementation of information technology software
(v) Agreeing to the obligation to refrain from an act, or to tolerate an act or a situation, or to do an act

(vi) Transfer of goods by way of hiring, leasing, licensing or in any such manner without transfer of right to use such goods
(vii) Activities in relation to delivery of goods on hire purchase or any system of payment by installments
(viii) Service portion in the execution of a works contract
(ix) Service portion in an activity wherein goods, being food or any other article of human consumption or any drink (whether or not intoxicating) is supplied in any manner as a part of the activity.

Part - B

1a) Computation of assessable value of excisable goods:

Particulars	Amount (₹)	Amount (₹)
Contracted sale price		10,00,000
Less:		
Excise duty (Note – 1)	1,11,200	
VAT (Note – 1)	37,000	
Octroi (Note – 1)	9,500	
Actual freight from "place of removal" to buyer premises (Note - 2)	42,300	2,00,000
Assessable value		8,00,000

Notes - In the given question, for the purpose of determining the assessable value of the excisable goods:-

1. the duty of excise, sales tax and other taxes, if any, actually paid or payable on the excisable goods has to be excluded [Section 4(3)(d) of the Central Excise Act, 1944].
2. the cost of transportation from the place of removal up to the place of delivery of the excisable goods has to be deducted [Rule 5 of the Central Excise Valuation (Determination of Price of Excisable Goods) Rules, 2000].
3. the cost of transportation, worth ₹ 27,000, from the factory to the place of removal would not be excluded [Explanation 2 to rule 5 of Central Excise Valuation (Determination of Price of Excisable Rules, 2000].
4. cost of packing, ₹ 4,000 and ₹ 9,000 would not be deducted. In this regard, it has been clarified that as per section 4 of the Central Excise Act, 1944,packing charges would form part of the assessable value whether packing is ordinary or special, or primary or secondary.
   Any charges recovered for packing are the charges recovered in relation to the sale of the goods underassessment and, hence, will form part of the transaction value of the goods[Circular no. 354/81/2000 dated 30/6/2000].
5. The cost of drawings and designs, worth ` 6,000 would not be deducted.[Rule 6 of Central Excise Valuation (Determination of Price of Excisable Rules, 2000].

b) Sahu & Co, a SSI unit will be entitled to exemption in the year 2013-14, if its turnover in the year 2012-13 was less than ₹ 400lakhs. As per Notification No.8/2003 CE dated 01.03.2003, which governs the provisions relating to small scale exemption, following items will not be included for calculating the turnover limit of ₹ 400 lakh of previous year:
   (i) Captive consumption in the manufacture of excisable goods
   (ii) Export to USA
   (iii) Job work done under Notification No.214/86 CE

Only the goods bearing the brand name of others, which are ineligible for the grant of SSI exemption, are excluded for the purpose of said limit. Since, goods manufactured in rural area with brand name of others are eligible for SSI exemption; the same will not be excluded for calculating the said limit.

Therefore, the turnover to be considered for the limit of ₹400 lakh will be computed as under:

Product	Clearance for home consumption	Export to Nepal	Goods manufactured in rural area with brand name of others	Total Turnover
AB	55	50	45	150
SA	40	40	35	115
AS	60	39	35	134
			Total	399

Since turnover of the unit during the year 2012-13 is less than ₹ 400 lakh, the unit is entitled to SSI exemption from excise duty in the year 2013-14.

2.

a) The Apex Court in the case of CCEx. v. Connaught Plaza Restaurant (Pvt) Ltd. 2012 (286) E.L.T. 321 (S.C.)considered the various submissions of the assessee as under:-

(i) The assessee quoted that as per the definition of "ice cream" under the Prevention of Food Adulteration Act, 1955 (PFA), the milk fat content of "ice-cream" and "softyice-cream" shall not be less than 10%. Hence, if the 'soft serve', containing 5% milk fat content is classified as "ice-cream", it would make the assessee liable to prosecution under the PFA. The SC observed that the definition of one statute (PFA) having a different object, purpose and scheme could not be applied mechanically to another statute (Central Excise Act). The object of the Excise Act is to raise revenue whereas the provisions of PFA are for ensuring quality control. Thus, the provisions of PFA have nothing to do with the classification of goods subjected to excise duty under a particular tariff entry.

(ii) The assessee submitted that "soft serve" could not be considered as "ice-cream" as it was marketed by the assessee world over as 'soft serve'.
SC rejected this averment on the ground that the manner, in which a product might be marketed by a manufacturer, did not necessarily play a decisive role in affecting the commercial understanding of such a product. What matters was the way in which the consumer perceived the product notwithstanding marketing strategies. An average reasonable person who walked into a "McDonalds" outlet with the intention of enjoying an "ice-cream", 'softy' or 'soft serve', could not be expected to be aware of intricate details such as the percentage of milk fat content, milk non-solid fats, stabilisers, emulsifiers or the manufacturing process, much less its technical distinction from "ice-cream".

(iii) The assessee pleaded that in the matters pertaining to classification of a commodity, technical and scientific meaning of the product was to prevail over the commercial parlance meaning. The Apex Court observed that none of the terms in Heading 04.04, Heading 21.05and Heading 2108.91 had been defined and no technical or scientific meanings had been given in the chapter notes. Further, 'soft serve' was also not defined in any of the said chapters. Supreme Court, after considering various judgments, concluded that in the absence of a statutory definition or technical description, interpretation ought to be in accordance with common parlance principle and not according to scientific and technical meanings.

(iv) The assessee contended that based on rule 3(a) of the General Rules of Interpretation which stated that a specific entry should prevail over a general entry, 'soft serve' would fall under Heading 04.04 since it was a specific entry. The Supreme Court rejecting this contention held that in the presence of Heading21.05 (ice cream), "ice cream" could not be classified as a dairy product under Heading 04.04. Heading 21.05 was clearly a specific entry.
Further, referring to a trade notice issued by the Mumbai Commissioner ate relating to classification of softy ice-cream being sold in restaurant etc. dispensed by vending machine, the Apex Court observed that the said trade notice indicated the commercial understanding of

'soft-serve' as 'softy ice-cream'.

In the light of the aforesaid discussion, the Apex Court held that' soft serve' was classifiable under Heading 21.05 as "ice cream" and not under Heading04.04 as "other dairy produce".

b) The Supreme Court in the case of CCEx., Mumbai v. Fiat India Pvt. Ltd. 2012 (283) E.L.T. 161 (S.C.)observed that as per section 4(1)(a) of the Central Excise Act, 1944, duty is paid on the "transaction value" in a case where the goods are sold by the assessee, for delivery at the time and place of the removal, the assessee and the buyer of the goods are not related and the price is the sole consideration for the sale. If any of these ingredients is missing, the price shall not be considered as transaction value.

Supreme Court opined that there was an extra commercial consideration in artificially depressing the price. Full commercial cost of manufacturing and selling was not reflected in the price as it was deliberately kept below the cost of production. Thus, price could not be considered as the sole consideration for sale. No prudent business person would continuously suffer huge loss only to penetrate market; they are expected to act with discretion to seek reasonable income, preserve capital and, in general, avoid speculative investments. It is immaterial that the cars were not sold to related persons.

The Apex Court therefore held that, in the instant case, the selling price could not be accepted as transaction value.

3. a)

MRP valuation shall apply under the Central Excise Act, 1944 if the following two conditions are satisfied cumulatively:

(i) The excisable goods to be valued are covered under the Legal Metrology Act,2009 or related rules or under any other law and such law requires declaration of the retail sale price on the package of such goods and

(ii) The Central Government has notified the said goods as goods in relation to which the payment of excise duty will be on the basis of the MRP less such deductions/abatements as it may allow in the notification.

b)

i) The said statement is not valid. Earlier, Rule 6(3C) of CENVAT Credit Rules,2004 provided that in case of services relating to life insurance, provider of output service was obligated to pay every month an amount equal to 20% of the credit availed on inputs and input services in that month. However, now Rule 6(3C) of CENVAT Credit Rules, 2004 has been omitted vide Notification No. 18/2012-(CE) NT dated 17.03.2012 and such obligation has been dispensed with.

ii) The proviso to rule 9 of the Central Excise Valuation (Determination of Excisable Goods)Rules, 2000 lays down that in a case where the related person does not sell the goods but uses or consumes such goods in the production or manufacture of articles, the value there of shall be determined in the manner specified in rule 8 of the Valuation Rules which provides that the value will be 110% of the cost of production or manufacture of such goods

Therefore, when the goods are sold to PQR Ltd., the assessable value shall be 110% of ₹ 16,000 (₹ 16,000 × 110%) i.e., ₹ 17,600.

However, in the instant case, if PQR Ltd. is an unrelated buyer, the assessable value will be the transaction value of the goods i.e. ₹ 20,000.

iii) Best judgment assessment: According to provisions of Section 72 of Finance Act, 1994 if any person, liable to pay service tax,—

(a) fails to furnish the return under section 70; OR

(b) having made a return, fails to assess the tax in accordance with the provisions of this Chapter or rules made there under, the Central Excise Officer, may require the person to produce such accounts, documents or other evidence as he may deem necessary and after taking into account all the relevant material which is available or which he has gathered, shall by an order in writing, after giving the person an opportunity of being heard, make the assessment of the value of taxable service to the best of this judgment and determine the sum payable by the assessee or refundable to the assessee on the basis of such assessment.

4.

a) The Supreme Court in case of Nicholas Piramal India Ltd. v. CCEx., Mumbai 2010 (260) E.L.T. 338 (S.C.)ruled that short shelf-life could not be equated with no shelf-life and would not ipso facto mean that it could not be marketed. A shelf-life of 2 to 3 days was sufficiently long enough for a product to be commercially marketable. Shelf-life of a product would not be a relevant factor to test the market ability of a product unless it was shown that the product had absolutely no shelf-life or the shelf-life of the product was such that it was not capable of being brought or sold during that shelf-life.

b) Goods which are not listed in Tariff or goods which are mentioned in Tariff, but the column of rate of duty is blank are non-excisable goods, e.g. water (there is no entry in Tariff). Excise law is not applicable on non excisable goods.

"Non-dutiable goods" are excisable goods listed in Excise Tariff. Excise law is applicable to them, but they are not liable to excise duty. Non dutiable goods may be of two types-

(i) Nil duty goods-Tariff rate for such goods is nil, and
(ii) Exempted goods-100% exemption is available under section 5A for such goods.

5 a)

i) According to the trade parlance test, if a product is not defined in the Schedule and Section Notes and Chapter Notes of the Central Excise Tariff Act, 1985, then it should be classified according to its popular meaning or meaning attached to it by those dealing with it, i.e., in commercial sense. However, where the tariff heading itself uses highly scientific or technical terms, goods should be classified in scientific or technical sense.

ii) Section 4(3)(b) of Central Excise Act, 1944 states that persons shall be deemed to be related if:
  (a) they are inter-connected undertakings;
  (b) they are relatives;
  (c) amongst them the buyer is a relative and a distributor of the assessee, or a sub-distributor of such distributor; or
  (d) they are so associated that they have interest, directly or indirectly, in the business of each other.

Note: "Relative" shall have the meaning assigned to it in clause (41) of section 2 of the Companies Act, 1956.

ii) The Central Excise Tariff Act, 1985 incorporates five Rules of Interpretation: Rule 3(c) of the Rules for the Interpretation provides that when goods cannot be classified by reference to rule 3(a) or rule 3(b), they shall be classified under the heading which occurs last in the numerical order among those which equally merit consideration. Thus the maxim "Latter the Better" applies in determining the classification of the excisable goods.

(OR)

5 b)

i)

S.No	Compounded levy scheme	Duty based on annual production capacity
1.	Rule 15 of the Central Excise Rules, 2002 provides for the compounded levy scheme.	Section 3A of the Central Excise Act, 1944 provides for the duty based on production capacity.
2.	Under compounded levy scheme, prescribed duty is paid for a specified period on the basis of certain factors relevant to production, like size of equipment employed, production capacity or some other criteria.	Under this scheme, prescribed duty is paid on the basis of annual production capacity of the factory.
3.	It is presently applicable to stainless steel pattas/patties and aluminum circles.	It is presently applicable to pan masala, unmanufactured tobacco, jarda scented tobacco and chewing tobacco.
4.	It is an optional scheme i.e., in respect of the goods covered under this scheme, the manufacturer can also opt to pay duty as per normal rules.	This scheme is compulsory i.e, in respect of the goods covered under this scheme, the manufacturer cannot pay duty in any other manner.

(ii) As per section 2(f) of the Central Excise Act, 1944 "manufacture" includes any process-

(i) incidental or ancillary to the completion of a manufactured product;

(ii) which is specified in relation to any goods in the Section or Chapter Notes of the First Schedule to the Central Excise Tariff Act, 1985 as amounting to manufacture, or

(iii) 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-Iabelling of containers including the declaration or alteration of retail sale price on it or adoption of any other treatment on the goods to render the product marketable to the consumer,

and the word "manufacturer" shall be construed 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 production or manufacture on his own account.

The processes that qualify to be manufacture as per clause (ii) and (iii) of section 2(f) are termed as deemed manufacture.

Thus, if any process which is specified in the Section or Chapter Notes of the First Schedule to the Central Excise Tariff Act, 1985 as amounting to manufacture is carried out, goods will be deemed as manufactured, even if as per Court decisions, the process may not amount to manufacture.

For instance, if any of specified processes (like re-packing,re-labelling, alteration of retail sale price etc.) is being carried out on goods covered in Third Schedule to the Central Excise Act, 1944, the process will be deemed as manufacture.