PRIME ACADEMY
40th SESSION PROGRESS TEST
ADVANCED MANAGEMENT ACCOUNTING

No of pages: 4 **Total Marks: 75**
Time Allowed: 2 Hrs

PART - A

I. Write short notes on the following. Provide examples:

a) Relevant cost
b) Absorption costing method for the valuation of finished goods inventory
c) Opportunity cost
d) Discretionary cost
e) Major areas of decision-making in which differential costing is used **(5 x 3=15 Marks)**

II. Pick out from each of the following items, costs that can be classified under 'committed fixed costs' or 'discretionary fixed costs".

(i) Annual increase of salary and wages of administrative staff by 5% as per agreement
(ii) New advertisement for existing products is recommended by the Marketing Department for achieving sales quantities that were budgeted for at the beginning of the year.
(iii) Rents paid for the factory premises for the past 6 months and the rents payable for the next six months. Production is going on in the factory.
(iv) Research costs on a product that has reached 'maturity' phase in its life cycle and the research costs which may be needed on introducing a cheaper substitute into the market for facing competition.
(v) Legal consultancy fees payable for patent rights on a new product Patenting rights have been applied for. **(5 x 1=5 Marks)**

III. Determine the selling price per unit to earn a return of 12% net on capital employed (net of Tax @ 40%).

The cost of production and sales of 80,000 units per annum are:

Material	₹ 4,80,000
Labour	₹ 1,60,000
Variable Overhead	₹ 3,20,000
Fixed overhead	₹ 5,00,000

The fixed portion of capital employed is ₹12 lacs and the varying portion is 50% of sales turnover. **(5 Marks)**

PART B **(50 Marks)**

Answer any five out of six questions below. Each question carried 10 Marks.

1. R.G. Ltd. has several product lines with a sales manager in charge of each product line and he is paid a bonus based on the net income generated by his product line. In analysis the performance of one product line, the General Sales Manager noted that the sales declined from ₹ 8 lakhs last year to ₹ 6 lakhs for the current year. However the product line manager received a larger than last year because net income increased from ₹ 90,000 last year to ₹ 1,20,000 for the current year.
The General Sales Manager wonders how the product line manager is entitled to a bonus with a decline in sales. He also wants to know how net income increased, when sales decline. As a Cost Accountant you are required to prepare the income statements, based which the bonus was paid. Explain with supporting figures why net income increased when sales declined. What do you think of the present method of paying the Bonus? Can you suggest some other method?
The data given in support for the bonus payment are:

	Year 2 ₹	Year 1 ₹
Units Sold @ ₹ 20	30,000	40,000
Standard Variable Cost of Production per unit (₹)	8	8
Fixed Factory Overhead Cost (₹)	2,00,000	2,00,000
Selling & Distribution Expenses (assumed to be fixed) (₹)	1,40,000	1,40,000
Standard Fixed Factory Overhead per unit (₹)	5	5
Units Produced	50,000	30,000
Units–Opening Finished Goods Inventory	-	10,000

All factory overhead variances are written off to cost of goods sold.

2. SFM Ltd. wants to evaluate the potential elimination of Division 'Z'. The basic information regarding cost and revenue is given below:

	Division X and Y ₹	Division Z ₹	Total ₹
Sales	₹ 1,20,000	₹ 15,000	₹ 1,35,000
Variable Expenses	(60,000)	(8,000)	(68,000)
Contribution Margin	60,000	7,000	67,000
Traceable Fixed Costs	(42,000)	(12,000)	(54,000)
Divisional Income	18,000	(5,000)	13,000
Unallocated Fixed Costs	---	---	(6,000)
Income before Taxes			7,000

(i) What will be the increase or decrease in profit by eliminating Division 'Z' if all costs traceable to division 'Z' are avoidable? Should the company eliminate?

(ii) Assume that executives and supervisory personnel in Division 'Z' will be reassigned to other divisions, if division is eliminated. Included in ₹ 12,000 of traceable fixed costs of Division 'Z' are ₹ 6,000 of salaries for these personnel. What is the effect of eliminating division 'Z' with this assumption?

(iii) Assume that fixed assets of Division 'Z' can be sold for ₹ 1,50,000 if Division 'Z' is eliminated. Remaining life of these assets is 10 years. Company can earn interest of 12% on invested funds. By what amount will this information affect the benefit to eliminate? [PVIFA (12%, 10) = 5.650]

3. Ret Ltd., a retail store buys computers from Comp Ltd. and sells them in retail. Comp Ltd. pays Ret Ltd. a commission of 10% on the selling price at which Ret sells to the outside market. This commission is paid at the end of the month in which Ret Ltd. submits a bill for the commission. Ret Ltd. sells the computers to its customers at its store at ₹ 30,000 per piece. Comp Ltd. has a policy of not taking back computers once dispatched from its factory. Comp Ltd. sells a minimum of 100 computers to its customers. Comp Ltd. charges prices to Ret Ltd. as follows:

- ₹ 29,000 per unit, for order quantity 100 units to 140 units.
- ₹ 26,000 per unit, for the entire order, if the quantity is 141 to 200 units. Ret Ltd. cannot order less than 100 or more than 200 units from Comp Ltd.

Due to the economic recession, Ret Ltd. will be forced to offer as a free gift, a digital camera costing it ₹ 4,500 per piece, which is compatible with the computer. These cameras are sold by another company, Photo Ltd. only in boxes, where each box contains 50 units. Ret Ltd. can order the cameras only in boxes and these cameras cannot be sold without the computer. In its own store, Ret Ltd. can sell 110 units of the computer. At another far of location, Ret Ltd. can sell up to 80 units of the computer (along with its free camera), provided it is willing to spend ₹ 5,000 per unit on shipping costs. In this market also, the selling price that each unit will fetch is ₹ 30,000 per unit. You are required to:

(i) State what is Ret's best strategy along with supporting calculations.

(ii) Compute the break-even point in units, considering only the above costs.

4. Tim-Tim Ltd. is manufacturing three products. The cost details are as follows:-

Particulars	Product A	B	C
	(₹)	(₹)	(₹)
Selling Price	35	40	50
Direct Materials (₹ 3 per unit)	12	15	18
Direct Labour	5	6	6
Direct Expenses	8	9	11
Contribution	10	10	15
No. of Units Sold	20,000	40,000	20,000
Contribution	2,00,000	4,00,000	3,00,000
Total Contribution			9,00,000
Less: Fixed Cost			7,50,000
Profit			1,50,000

The direct materials were all imported. Due to foreign exchange restrictions, henceforth, the company can import only 3,00,000 units of raw materials. The company can produce in all 1,00,000 units maximum (all products). However, they can market only 20,000 units of products A & C each. There is a local substitute material which is available at a price of ₹ 3.75 per unit. Besides, the company has to spend ₹ 50,000 on intermediaries and consumables, if local substitute material is used in the production process. There was also a third party who was willing to take a part of the plant on lease upto 50,000 units capacity of B and willing to pay lease charges of ₹ 2,75,000. You are required to advise the management:

(i) What should be the quantum of production/sales mix of products with existing import restrictions?

(ii) Whether the company can optimise production of 1,00,000 units with local substitute materials?

(iii) Whether the company can enhance profits by leasing out a part of the plant to the third party and restricting its own production?

5. The details of the output presently available from a manufacturing department of Hitech Industries Ltd. are as follows:
   - Average output per week 48,000 units from 160 employees
   - Saleable value of output ₹ 6,00,000
   - Contribution made by the output towards fixed expenses and profit. ₹ 2,40,000

   The Board of Director plans to introduce more automation in the department at a capital cost of ₹ 1,60,000. The effect of this will be to reduce the number of employees to 120, but to increase the output per individual employee by 60%. To provide the necessary incentive to achieve the increased output the Board intends to offer a 1% increase in the piece work rate of one rupee per article for every 2% increase in average individual output achieved. To sell the increased output, it will be necessary to decrease the selling price by 4%.

   Required:

   Calculate the extra weekly contribution resulting from the proposed change and evaluate, for the Board's information, the worth of the project.

6. X is a multiple product manufacturer. One product line consists of motors and the company produces three different models. X is currently considering a proposal from a supplier who wants to sell the company blades for the motors line. The company currently produces all the blades it requires. In order to meet customer's needs, X currently produces three different blades for each motor model (nine different blades).

The supplier would charge ₹ 25 per blade, regardless of blade type. For the next year X has projected the costs of its own blade production as follows (based on projected volume of 10,000 units):

- Direct materials ₹ 75,000
- Direct labour ₹ 65,000
- Variable overhead ₹ 55,000
- Fixed overhead
- Factory supervision ₹ 35,000
- Other fixed cost ₹ 65,000
- Total production costs ₹ 2,95,000.

Assume (1) the equipment utilized to produce the blades has no alternative use and no market value, (2) the space occupied by blade production will remain idle if the company purchases rather than makes the blades, and (3) factory supervision costs reflect the salary of a production supervisor who would be dismissed from the firm if blade production ceased.

(i) Determine the net profit or loss of purchasing (rather than manufacturing), the blades required for motor production in the next year.

(ii) Determine the level of motor production where X would be indifferent between buying and producing the blades. If the future volume level were predicted to decrease, would that influence the decision?

(iii) For this part only, assume that the space presently occupied by blade production could be leased to another firm for ₹ 45,000 per year. How would this affect the make or buy decision?

PRIME ACADEMY
40th SESSION – FINAL - PROGRESS TEST
ADVANCED MANAGEMENT ACCOUNTING
SUGGESTED ANSWERS
PART - A

I.

a) Relevant cost: Relevant Cost: Expected future costs which differ for alternative course. It is not essential that all variable costs are relevant and all fixed costs are irrelevant. Fixed, or variable costs that differ for various alternatives are relevant costs. Relevant costs draw our attention to those elements of cost which are relevant for the decision.
Example:
Direct Labour under alternative I – ₹ 10/ hour
Direct Labour under alternative II – ₹ 20/hour
Then, Direct Labour is Relevant Cost.

b) Absorption costing method for the valuation of finished goods inventory: When absorption costing method is used, production fixed overheads are charged to products and are included in product costs. Consequently, the closing stocks are valued on total cost (including fixed overheads) basis. The net effect is that the charge of fixed overheads to P/L account gets reduced, if the closing stock is greater than the opening stock. This situation has the effect of inflating the profit for the period.
Where stock levels are likely to fluctuate significantly, profits may be distorted if calculated on absorption costing basis. If marginal costing is used, since the fixed costs are charged off to P/L account as period cost, such a situation will not arise.

c) Opportunity cost: Opportunity cost is a measure of the benefit of opportunity forgone when various alternatives are considered. In other words, it is the cost of sacrifice made by alternative action chosen. For example, opportunity cost of funds invested in business is the interest that could have been earned by investing the funds in bank deposit.

d) Discretionary cost: Discretionary costs can be explained with the help of following two important features-
(i) They arise from periodic (usually yearly) decisions regarding the maximum outlay to be incurred.
(ii) They are not tied to a clear cause and effect relationship between inputs and outputs.
Examples of Discretionary Costs includes: advertising, public relations, executive training, teaching, research, health care and management consulting services. The note worthy feature of discretionary costs is that managers are seldom confident that the "correct" amounts are being spent.

e) Major areas of decision-making in which differential costing is used: levels of activities are being considered, or while choosing between competing alternatives differential cost analysis is essential. The differential cost is useful for decision making in the following areas:
(i) Capital Expenditure Decisions.
(ii) Make or Buy Decision
(iii) Production Planning
(iv) Sales Mix Decision
(v) Production or Product Decision
(vi) Change in Level or Nature of an Activity.

II.

Committed Fixed Cost	Discretionary Fixed Cost
(i) Salary and Wage increase.	(ii) New Advertisement Cost.
(iii) Rents payable for the next 6 months.	(iv) Research Cost for substitutes.
(v) Legal Fees for filing for patent rights.	

III.

Return of 12% Net (after tax of 40%) on Capital Employed is equivalent to 20% (Gross) [12% ÷ (1 – 0.4)] on Capital Employed.

Let Selling Price per unit to be 'K'

Since Total Sales = Total Cost + Profit

80,000 K = ₹ 14,60,000 + 20% (12,00,000 + 0.5 × 80,000K)

Or, 80,000 K = ₹ 14,60,000 + 2,40,000 + 8,000K

Or, 72,000 K = ₹ 17,00,000

Or, 'K' = ₹ 17,00,000

₹ 72,000

= ₹ 23.61

Hence Selling Price per unit will be ₹23.61.

PART B

1. Income Statements

(Based on which bonus was paid)

(Amount in ₹)

	Year 1	Year 2
Units Sold	40,000	30,000
Sales @ ₹ 20 per unit	8,00,000	6,00,000
Cost of Sales:		
Variable Cost		
Year 1 : 30,000 @ ₹ 8	2,40,000	---
Year 2 : 50,000 @ ₹ 8	---	4,00,000
Fixed Factory Overhead	2,00,000	2,00,000
Cost of Production	4,40,000	6,00,000
Add: Opening Stock		
Year 1 : 10,000 @ ₹ 13	1,30,000	---
Year 2 : Nil	---	---
Less: Closing Stock:	5,70,000	6,00,000
Year 1 : Nil	---	---
Year 2 : 20,000 @ ₹ 13	---	2,60,000
Cost of Goods Sold	5,70,000	3,40,000
Add: Selling and Distribution Expenses	1,40,000	1,40,000
Cost of Sales	7,10,000	4,80,000
Income	90,000	1,20,000

In the above statements income in year 2 increased in spite of decrease in sale because fixed overheads have been carried over to next year as part of the value of closing stock in year 2. The above method of paying bonus to sales manager cannot be considered appropriate. It may be appropriate to pay bonus to production manager. The relevant method for paying bonus to sales manager is the contribution method as shown below:

	Year 1	Year 2
	(₹)	(₹)
Sales	8,00,000	6,00,000
Less: Variable Cost	3,20,000	2,40,000
Contribution	4,80,000	3,60,000
Less: Fixed Cost	3,40,000	3,40,000
Income	1,40,000	20,000

If bonus to sales manager is paid on the contribution method, sales manager cannot get more bonus when sales decline.

2. (i) Statement showing comparative profits assuming that costs traceable to Division Z are avoidable

Particulars	Total Company Operations, if it Keeps Z (₹)	Eliminates Z (₹)	Benefit / (Cost) to eliminate Z (₹)
Sales	1,35,000	1,20,000	(15,000)
Variable Expenses	(68,000)	(60,000)	8,000
Contribution	67,000	60,000	(7,000)
Total Fixed Cost	(60,000)	(48,000)	12,000
Profit	7,000	12,000	5,000

Advantages to Eliminate Division Z:	(₹)
Reduction in Variable Expenses	8,000
Reduction in Fixed Expenses (₹ 12,000 – ₹ 6,000)	6,000
Total Benefit	14,000
Disadvantages to Eliminate Z:	(₹)
Reduction in Sales	15,000
Decrease in Profit by Eliminating Division Z	1,000

₹ 26,549 should be added to the annual benefits of eliminating Division Z. The equivalent annual cash flow of ₹ 26,549 is computed by using annuity table for an assumed annuity of ten years at 12% with present value of ₹ 1,50,000. Cash Flow ₹26,549 (₹ 1,50,000 ÷ 5.650). The equivalent annual cash flow of ₹ 26,549 is the opportunity cost of keeping division Z or alternatively it is a benefit from eliminating the division Z.

3.

Particulars *Order Qty 100-140 (₹)*Order Qty 141-200 (₹)

I. Selling Price / unit *30,000 *30,000
II. Commission @ 10% *3,000 *3,000
III. Sales Revenue p. u. [I + II] *33,000 *33,000
IV. Less: Variable Purchase Cost *29,000 *26,000
V. Contribution / unit before shipping [III – IV] *4,000 *7,000
VI. Less: Shipping Cost (Sales > 110 units) *5,000
VII. Contribution/ units after Shipping [V – VI] *2,000

(i) Upto 110 units, Ret Ltd. will earn a contribution of ₹ 4,000 per unit.
(ii) Between 110 & 140 units, contribution of ₹ 4,000 will be wiped out by ₹ 5,000 on shipping costs. Hence we should not consider 110 – 140 range.
(iii) 101 – 110 not to be considered since additional costs of ₹ 2,25,000 on purchase of cameras will not be covered by 10 units.
(iv) Valid consideration, 100 units or 141 to 190 units.

		100 Units	141 Units	150 Units	190 Units
A	No. of Camera Boxes	2 (₹)	3 (₹)	3 (₹)	4 (₹)
B	Cost of Cameras (₹)	4,50,000	6,75,000	6,75,000	9,00,000
C	Contribution(₹4,000/u)	400,000	---	---	---
D	Contribution on first 110 units @ ₹7,000/u	---	7,70,000	7,70,000	7,70,000
E	Contribution on balance units @ ₹2,000/u	---	62,000	80,000	1,60,000
F	Total Contribution (C)+(D+(E)	4,00,000	8,32,000	8,50,000	9,30,000
G	Profit (₹) …(F) – (B)	(50,000)	1,57,000	1,75,000	30,000

Best strategy will be to buy 150 units from Comp. Ltd., and sell 110 units at store and remaining 40 units in outside.

Break –even Point (BEP) should be between 151 – 191 units:

Extra Camera Box Cost beyond 150 units ₹ 2,25,000
Less: Profit for 150 units ₹ 1,75,000
Extra Profit to be earned ₹ 50,000
No. of units to cover this additional costs at contribution 25 units (50,000/2,000)
BEP 175 units (150 units + 25 units)

4.

(i) Statement of Quantum of Production / Sales Mix of Products (with existing import restrictions)

Products	A	B	C
Selling Price per unit (₹)	35	40	50
Less: Variable Cost per unit (₹)	25	30	35
Contribution per unit of Product (₹)	10	10	15
Units of Materials	4	5	6
Contribution per unit of Materials (₹)	2.50	2	2.50
Ranking	I	II	I
Units Made	20,000	20,000	20,000
Material Consumed	80,000	1,00,000	1,20,000
Contribution (₹)	2,00,000	2,00,000	3,00,000
Total Contribution (₹)			7,00,000
Less: Fixed Costs (₹)			7,50,000
Profit / (Loss) (₹)			(50,000)

(ii) Use of Local Substitute of Material (Output: 1,00,000 units)

Contribution per unit of Product B on using Local Substitute Material (₹ 10–₹ 3.75)	6.25
Total Contribution on 40,000 units of Product B (40,000 units × ₹ 6.25)	2,50,000
Less: Intermediaries Expenses	50,000
Net Additional Contribution	2,00,000
Less: Loss on Present Output of 60,000 units as per (i)	50,000
Net Profit	1,50,000

Thus, the company can have optimum production of 1,00,000 units by using local substitute of material.

(iii) Evaluation of Leasing Out a part of the Plant

Total Contribution on Sale of 20,000 units of Products A and C and 10,000 units of Product B by using imported material (20,000 units × ₹ 10 + 10,000 units × ₹ 10 + 20,000 units × ₹ 15)	6,00,000
Less: Fixed Costs	7,50,000
Profit / (Loss)	(1,50,000)
Add: Lease Rent Received	2,75,000
Net Profit	1,25,000

Conclusion:
The net profit is ₹ 1,50,000 in case the company uses local substitute of material and the plant capacity fully for producing 1,00,000 units, whereas by leasing out the plant capacity up to 50,000 of Product B for a rent of ₹ 2,75,000, the company makes a profit of ₹ 1,25,000. A comparative study of the two alternatives suggests that it will be better for the company to have optimum production of 1,00,000 units by using local substitute of material.

5. Evaluation of the Project for the Board's information and Computation of Extra Weekly Contribution from Automation

Sales (units) [W.N.-1]	57,600
	(₹)
Sales Value (57,600 units × ₹ 12) [W.N.-3]	6,91,200
Less: Marginal Cost Excluding Wages (57,600 units × ₹ 6.50) [W.N.-4]	3,74,400
Wages (57,600 × ₹ 1.30) [W.N.-2]	74,880
Marginal Contribution	2,41,920
Less: Present Contribution	2,40,000
Extra Weekly Contribution	1,920

Payback Period for recovering the capital cost is 83.33 Weeks (₹ 1,60,000 / ₹ 1,920)

Recommendation

The project can be taken up presuming that increase in overhead, if any, will be less than the increase in contribution as computed above.

Working Notes

1. Present Output per employee and Total Future Expected Output:

   Present Output per employee = Total Present Output/Total Number of Present Employees
   = 48,000 units/160 employees
   = 300 units

   Estimated Future Output = Total Number of Future Employees × Present Output per employee + 60 % of Present Output
   = 120 × (300 units + 60% × 300 units)
   = 57,600 units

2. Present and Proposed Piece Work Rate:

   Present Piece Work Rate = ₹ 1 per unit
   Proposed Piece Work Rate = Present Piece Work Rate + 30%
   = ₹ 1 + 0.30
   = ₹ 1.30 per unit.

3. Present and Proposed Selling Price per unit:

   Present Selling Price per unit = ₹ 12.50 (₹ 6,00,000 / 48,000 units)
   Proposed Selling Price per unit = ₹ 12 (₹ 12.50 – 4% × ₹ 12.50)

4. Present Marginal Cost Excluding Wages per unit:

   = Present Sales Value - Contribution towards (Fixed Expenses & Profit) - Present Wages Present Output (Units)
   (= 6,00,000 - 2,40,000 - 48,000)/48,000 units
   = ₹6.50 per unit

6.

This is a make or buy decision so compare the incremental cost to make with the incremental cost buy.

Incremental Costs Per Unit (₹)	
Direct Materials (₹ 75,000 ÷ 10,000 units)	7.50
Direct Labour (₹ 65,000 ÷ 10,000 units)	6.50
Variable Overhead (₹ 55,000 ÷ 10,000 units)	5.50
Supervision (₹ 35,000 ÷ 10,000 units)	3.50
Total Cost	23.00

Compare the cost to make the blades for 10,000 motors. ₹ 23.00, with the cost to buy, ₹ 25.00. There is a net loss of ₹ 2.00 if 'X' chooses to buy the blades.

'X' will be indifferent between buying and making the blades when the total costs for making and buying will be equal at the volume level where:
Variable Cost per unit × No. of units + Avoidable Fixed Cost = Cost of Buy Variable Cost per unit (DM + DL + VO) × No. of units + Factory Supervision Cost = Buying Cost per unit × No. of units
Let No. of in units = U
(₹ 7.50 + ₹ 6.50 + ₹ 5.50) × U + ₹ 35,000 = ₹ 25.00 U
₹ 19.50 U + ₹ 35,000 = ₹ 25.00 U
₹ 25.00 U – ₹ 19.50 U = ₹ 35,000
₹ 5.50 U = ₹ 35,000
U = 6,364 units of blades
As volume of production decreases, the average per unit cost of in house production increases. If the volume falls below 6,364 motors, then 'X' would prefer to buy the blades from the supplier.

(iii) If the space presently occupied by blade production could be leased to another firm for ₹ 45,000 per year, 'X' would face an opportunity cost associated with in house blade production for the 10,000 units of ₹ 4.50 per unit.
New Cost to Make = ₹ 23.00 + ₹ 4.50
= ₹ 27.50
Now 'X' should buy because the cost to make, ₹27.50, is higher than the cost to buy, ₹25.00.

PRIME ACADEMY
40th SESSION - PROGRESS TEST
INFORMATION SYSTEM CONTROL AND AUDIT

No of Page: 1 **Total Marks : 75**

PART - A **Time Allowed: 2Hrs**

1. ______________ is the first stage in SDLC
2. Process of planning the new systems or systems to replace/support existing system is called__________
3. The three broad steps in preliminary investigation are ______, __________ and _________
4. The process of ensuring that the software doesnot fail and it runs according to specifications given by users is called _________
5. _____ is an effort to adapt to changing user and business needs
6. In the absence of software baselining, there is a risk of ____________
7. ____________ is a usable system or system component which is built quickly at lesser cost and with an intention of being modified or replaced with a full fledged system.
8. ______ heads the project team and is responsible for day to day running of the project
9. _________________ and ___________________ are the responsibility of IT Steering committee
10. ___________ is concerned with the internal structuring of the database
11. ______________ implies that the new system should be capable of being used by the final users.
12. _____________ involves judging the incremental costs and benefits of the implementing the new system
13. ____________ captures the characteristics of data elements and their relationship amongst them.
14. _________ is used to automate activities that humans do to develop a system
15. The deliverable of the requirement analysis phase is _________________
16. ______________ refers to how data is organised within a database
17. In output design, __________ refers to way content is presented to users
18. When the purpose of information system is management decision making and multiple applications share the same data, _________ approach to data storage is recommended.
19. The three methods of validating vendors proposals are __________, ___________ and ________
20. Identifying and correcting syntax errors and diagnostic errors is called _____________

(25 x 1 = 25 Marks)

PART B

Answer any 5 Questions **(50 Marks)**

1. a) There are many reasons why Organisations fail to achieve systems development objective- Explain **(6 Marks)**
b) Explain two primary modes of data collection for Preliminary investigation **(4 Marks)**

2. a) What are the contents of User Requirement Specification Document **(4 Marks)**
b) Explain any four factors to be considered while designing data output **(4 Marks)**
c) Explain the term Unit Testing **(2 Marks)**

3. a) Explain meaning, advantage and limitations of any 3 migration strategies **(6 Marks)**
b) Explain the different types of system maintenance **(4 Marks)**

4. a) Explain the scenarios under which prototyping approach is considered useful **(6 Marks)**
b) What are the advantages of a pre-written application software **(4 Marks)**

5. a) Explain the role of File Librarian and LAN Administrator **(4 Marks)**
b) Explain the terms operational evaluation and information evaluation **(4 Marks)**
c) Explain the term Recovery Testing **(2 Marks)**

6. a) Explain the term software base lining and scope creep **(4 Marks)**
b) What type of training is to be imparted to system operators and users **(4 Marks)**
c) List 6 stages of SDLC **(2 Marks)**

PRIME ACADEMY
40th SESSION – FINAL - PROGRESS TEST
INFORMATION SYSTEM CONTROL AND AUDIT
SUGGESTED ANSWERS
PART - A

1	Preliminary Investigation/ Feasibility Study
2	System Design
3	Request Clarification, feasibility study, approval of request
4	System Testing
5	System Maintenance
6	Scope Creep
7	Prototype
8	Project Manager
9	Identification of viable projects, committing resources
10	Data Base Administrator
11	Operational Feasibility
12	Economic Feasibility
13	Data Dictionary
14	CASE Tools
15	User Requirement Specification/System Requirement Spec.
16	Internal Schema/Physical Schema
17	Form
18	Centralized Data Base
19	Checklists, point scoring analysis, public evaluation reports
20	Debugging

PART B

1. a) There are many reasons why Organisations fail to achieve systems development objective- Explain-
Some reasons which can be attributed for failure of systems development objective are:

1. Lack of senior management effort and involvement:
   - Developers and users watch as to which projects are getting senior manager attention. They would shift focus from projects they feel is not getting the required attention of top management.
   - Also it is the top management which commits resources to the projects and controls its progress.
2. Shifting user needs (called as scope creep- due to lack of software base lining)
   - User requirements for information systems keep changing. More changes imply more requests for systems development and more development projects.
   - Also if changes occur during development effort, there would be no baseline and developers find it very difficult to provide for every change request.

   Ex: Say a accounts software is in the process of development. A user request comes asking for additional report generation not stated in earlier requirement specification. When this development is being done another user may come with further requests and so on, there is no end to it.

3. Development of unstructured or strategic systems.
   - The requirements, specification and objectives of strategic systems are difficult to define and hence it would be difficult to determine if development effort is successful or not.(Ex: Expert Systems)
4. New technologies
   - When management tries to leverage new technology to its competitive advantage, it may face a problem that personnel are not familiar with the technology.

   Ex: An organization may want to achieve good results by implementing an ERP package, but may face a problem if users' do not know how to use the package.
5. Lack of standard project management and systems development methodologies.
   - Lack of formal project management methodologies makes it difficult to stick to time schedules/budget schedules.
6. Over-worked or under-trained development efforts.
   - Systems development team is over-worked due to constant requests
   - Most of the company's do not invest in employee training and hence the employees are not up-date on current technologies.
7. Resistance to change
   - Any development effort is countered by resistance to change.
   - If employees perceive that as a result of business process re-engineering their power position will be affected or that there may be "down-sizing/retrenchment" they will work against the development effort.

     <u>Example:</u> When computers were introduced in banks, in the early stages it faced lot of resistance from employee unions who felt it would adversely affect their job security.
8. Lack of user participation
   - If users are not involved in the development efforts, they may not feel responsible for the success of the projects. Also there may be resistance to change.
   - Hence user involvement is critical to the success of the project.
9. Inadequate testing and user training.
   - If new systems are not tested properly, they may not meet the business objectives. Also it may give rise to control risks.

     End user training on the new system is critical since any system is only as effective as the user who uses it

b)

Data collection could be done in two ways:

i. Review of internal documents   ii. Interviewing users

i. Review of internal documents:

- The analyst reviews internal documents like organizational charts and studying the operational / procedural document
- The purpose is to understand about the organisation and the problems it is currently facing.
- Ex: Study the existing pay-roll system to find out the information source and the reports generated.

ii. Interview users

- To understand the merits of the new/proposed system and the users opinion on the current system in use.
  To understand better about the nature of request and the reasons why users have submitted the same.

2. a) The deliverable of the requirement analysis phase is a comprehensive document called User Requirement Specification Document (URS) or System Requirement specification Document(SRS). This document contains details like:
   - the information requirement of the new system
   - the functional description which diagrammatically represents the features and its linkage,
   - the interactions of this system with other systems or modules
   - the acceptance criteria-i.e the test criteria that the system should pass for users to accept it
     This document would be signed-off by users in acceptance of the fact that all their requirements are correctly and completely reflected in the URS/SRS. IT Dept. would also sign-off on this document as an acknowledgement of their having understood the requirements and promising to deliver the same.

   b) Important factors to be considered in output design

Six important factors to be given importance while designing user outputs:

Content | Form | Output Volume | Timeliness | Media | Format

i. Content:

Meaning: Refers to actual data included in the outputs given in the report.
Ex: Content of the stock reports – S.No., Item code, Item description, Quantity etc.
Factor to be considered

- Too much content → managers waste time in identifying the relevant information needed → reduces the real use/impact of important information → hence only required information should be given in the outputs.
  (Implies that redundancies in data should be reduced)

ii. Form:

Meaning: Refers to way the content is presented to users
Ex: Quantitative, text, graphs, audio, video etc.
Factor to be considered

- Form of output should be as per requirement of individual users.
- Departmental managers usually require both summary and detailed information to be presented in relative terms (like charts, graphs etc) rather than in absolute terms. It helps in easy understanding of the data and hence better decisions.

iii. Output volume:

Meaning: Amount of data required at any one time
Factor to be considered

- If volume of data is heavy, it is preferable to have a high speed printer/rapid retrieval display unit.
- If unusually high volumes of outputs are to be generated, printing on paper may cost high. As an alternate organisations should look for other output media like computer output microfiche/tapes.

iv. Timeliness:

Meaning: Refers as to when the users require the output. It may be on periodic basis (weekly, monthly) or on request

Factor to be considered

- If rapid/ real-time outputs are required as in case of say railway/airline ticket booking systems, it is better to use communications-oriented and real-time systems.
- In DSS or MRS, user oriented 4GL tools effective as they provide a time sensitive alternate to tackle application back-logs/delays in software development.

v. Media:

Meaning: Refers to the physical devices used for input, output and storage.

Variety of media is available like paper, video display, and tapes/disks. Organisations should choose the medium best suited to their user requirements.

Ex: Banks use CDs/DATS to take back-up of their branch information.

vi. Format:

Meaning: Refers to the manner in which the data are physically arranged in the output.

Earlier, design tools like printer spacing charts were used to design outputs for managers/users. Currently prototyping 4GLs can be used to develop report prototypes quickly.

c)

Unit Testing

Unit refers to the smallest testable part of an application software.
This kind of tests are carried out by programmers to check individual units of the source code – to check if the unit meets the design and works as intended. Its objective is to ensure that each isolated component is correct.

3. a)

Conversion method	Meaning	Advantages	Limitations
1. Direct change over method (also called Plunge method)	On a specified date old system is dropped and new system is put to use Can be adopted only if extensive testing done beforehand	Users straight away use the new system-adaptation easy.	1. Risky 2. Long delays if errors occur since this the only system available to do the processing 3. Users resent/resist since unfamiliar system 4. Cannot compare results with the old system(since old system has been discarded)
2. Parallel conversion	Running the old system and the new system in parallel at the same time Results of the new system compared with that of the	1. Since data available from both old and new systems, any errors in new system can be corrected. 2. Users feel secure as they are not faced with abrupt change	1. Cost of running both systems (old and new) is very high. 2. Employees work load increases during conversion. 3. Unless new system is replacing old manual system, output

	old system and if reliable over a period of time, old system is stopped and new system put to use.		comparison difficult. 4. If new system is an improvement over existing system, outputs would differ and hence difficult to compare. 5. Users familiar with old system and will continue to use only that.
3. Gradual conversion	Attempts to combine the good features of parallel and direct changeover method. Volume of transaction gradually increased ➔ new system is phased in.	Users can use the new system gradually and there is a possibility of detecting and correcting errors without much system downtime.	1. Time consuming as it may take a long time to put the new system in use. 2. Not the best method for small, simple systems.
4. Modular prototype conversion	Involves building of modular, operational prototypes to change from old to new system. Each module is modified, accepted and put to use gradually.	1. Thorough testing of modules before being put to use. 2. User familiarity before model put to use.	1. Too many prototypes and hence may not be feasible. 2. Interfacing of the various modules (so that they work as a system) may be a problem.
5. Distributed conversion (Also called as PILOT run)	Involves full implementation of the system in one branch of the organization (say a bank branch) using any of the above four methods. If successful then carried out at other branches.	Problems if any can be identified and controlled in one location rather than affecting all locations.	Each branch/site may have its own problem that needs to be handled separately. Hence success in one site does not necessarily mean success in other sites.

b)

Category	Meaning	Example
Schedule maintenance	Maintenance efforts which can be anticipated and which are planned for	Implementation of new tax rates in payroll software after every budget
Rescue maintenance	Not anticipated – require immediate attention – may be some previously unnoticed errors/bugs	A particular screen in the billing module may not work. The system may stop processing and hence may require immediate attention.
Corrective Maintenance	To correct errors and bugs noticed in program	Microsoft patch release for bug in operating system
Adaptive maintenance	To tune the software to changes in its environment with which it interfaces	Changes in software to accept IP Version 6.0 addressing

4. a)

Users do not understand their information needs very clearly- experimenting with the prototype they may identify additional requirements which they may have overlooked or forgotten

ii. **System requirements are hard to define-**like in case of decision support systems which deal with un-structured or semi-structured decision environment.

iii. **The new system is mission critical or needed quickly-** hence considering the time constraint cannot go through the entire steps as stated in the traditional approach- hence need to build a prototype.

iv. **Past interactions between users and designers have resulted in misunderstanding-** hence better give the users a prototype to experiment with and receive their feedback.

v. **There is high risk of developing and implementing a wrong system -** hence it is better to experiment with a prototype which is less costly, obtain all requirements correctly and then go in for the final system.

b)

S. No.	Points for consideration	Advantage if we buy the software	Disadvantage if it is developed in-house
1.	**Implementation**	Rapid implementation	May take months or years to implement
2.	**Risk**	Low risk- product already available- organisation aware of the features it is going to get at what price.	Long development time- leads to uncertainty as regards quality and cost of development.
3.	**Quality**	Vendors dealing in application software- retain specialists who have lot of experience. Hence product quality good.	In-house programmers have to work on a wide range of applications and may not have expertise.
4.	**Cost**	Software vendors sell products to various customers and hence cost per customer may be low.	There may be some hidden costs.

5. a)

1	File Librarian	Responsible for managing the program and data files of an organisation. Ensures that files are issued, stored and retrieved securely.
2	LAN Administration	Overall control over the local area network- managing links, network components, LAN configuration back-ups etc.

b)

i. Development evaluation:

- This is done to see if system was developed **within schedule and within budgeted amount.** This requires budgets and schedules to be decided in advance and record of all costs are to be maintained.
- But many information systems skip schedules /overshoot budgets as they may have been **developed without well planned schedules/budgets** and **may have been not subjected to management control procedures.**

ii. Operation evaluation:

- It is evaluation of the system's hardware, software and personnel to see if they are capable of performing their duties and whether they do actually perform them.
- It may be easy to undertake if **criteria of evaluation** laid down clearly in advance.
  Ex: For payroll software if the criteria is it should process salary of 1000 employees per hour, when it is run in live area this can be checked at the time of monthly pay-roll run.
- It answers questions like:
  - ✓ Are all transactions processed on time?
  - ✓ Is the system computing values correctly?
  - ✓ Is the system response time within limits?

c) This testing is to understand the ability of a system to recover from a system failure. This is also referred to as crash-restart testing- which tests different aspects of a system failure and its ability to recover within acceptable time.

6. a) Shifting user needs (called as scope creep- due to lack of software base lining)

- User requirements for information systems keep changing. More changes imply more requests for systems development and more development projects.
- Also if changes occur during development effort, there would be no baseline and developers find it very difficult to provide for every change request.

Ex: Say a accounts software is in the process of development. A user request comes asking for additional report generation not stated in earlier requirement specification. When this development is being done another user may come with further requests and so on, there is no end to it.

b) **Training of systems operators**

- System operators are responsible for keeping equipment running + providing support services.
- Training should cover all types of operations; both routine and extra-ordinary.
- Areas of training should include :
  - ✓ How to switch on a new equipment
  - ✓ What are the normal operations of the new system
  - ✓ What are the common malfunctioning/problems that might arise, how to recognize them and what action is to be taken **(trouble shooting).**

- ✓ Who are the contact persons in case of unusual problems, how to get in touch with them (**Ex:** Vendor help desk number etc.)

Training of users

- ✓ It may involve **use of equipment** i.e. how to operate the system.
- ✓ They may be trained in **trouble-shooting.** This involves identification as to whether a problem is caused due to software or is it a hardware problem.
- ✓ They are also trained in **data handling.** This includes data editing, data coding, designing queries and deleting records.
- ✓ Users are trained in **system maintenance activities** like preparing disks, loading papers in printers and changing printer cartridges/ribbons.

c) Preliminary investigation, requirement analysis, design, development, testing, implementation.

PRIME ACADEMY
40th SESSION - PROGRESS TEST
DIRECT TAX LAWS

No. of pages: 3 **Total Marks: 65**
Time Allowed: 2 Hours

PART - A
Question 1 is Compulsory. Answer any 3 from the rest.
Working notes should form part of the answer
Wherever necessary suitable assumptions may be made by the Candidates

1

a. Mr. I an Indian citizen is a CFO of a company based in Chennai. During the previous year 14-15 he was out of India for a period of 200 days. He makes frequent visits outside India in connection with his employment. He wants to file his income tax return for the AY 15-16 as a non-Resident. Can he do so? Assume he has stayed for more than 365 days in the preceding 4 years. **(4 Marks)**

b. Mr. X is a Member of Legislative Assembly. He underwent an open heart surgery abroad in respect of which he received INR 5 Lacs from the State Government towards reimbursement of his medical expenses. The Assessing Officer contended that such amount is taxable as a perquisite under section 17. Discuss the correctness of the contention of the Assessing Officer. **(4 Marks)**

c. Vishnu has two houses, both of which are self-occupied. The particulars of the houses for the P.Y. 2014-15 are as under:

Particulars	House I ₹	House II ₹
Municipal valuation p.a.	8,00,000	12,00,000
Fair rent p.a.	6,00,000	14,00,000
Standard rent p.a.	7,20,000	14,80,000
Date of completion	31.3.2007	31.3.2010
Municipal taxes paid during the year	20%	18%
Interest on money borrowed for construction of house	3,50,000	5,00,000

Compute Vishnu's income from house property for A.Y.2015-16 and suggest which house should be opted by Vishnu to be assessed as self-occupied so that his tax liability is minimum. **(6 Marks)**

d. Mr. D received a vacant site as gift from his friend in November 2002. The site was acquired by his friend for Rs 3,64,000 in April 1990. D constructed a residential building during the year 2004-05 in the said site for ₹9,60,000. He carried out some further extension of the construction in the year 2007-08 for 5,51,000.D sold the residential building for ₹ 55,00,000 in January 2015 but the State stamp valuation authority adopted ₹ 65,00,000 as value for the purpose of stamp duty. Compute his long term capital gain, for the assessment year 2015-16 based on the above information. (Cost Inflation Index: FY 1990-91- 182; FY 2002-03 – 447, FY 2004-05- 480; FY 2007-08- 551; FY 2014-15 – 1024) **(6 Marks)**

2 (a) Mr. Hari has acquired a residential house property in Delhi on 1st April, 2005 for ₹ 9,94,000 and decided to sell the same on 3rd May, 2014 to Ms. Pari and an advance of ₹ 2,50,000 was taken from her. The balance money was not paid by Ms. Pari and Ms. Hari has forfeited the entire advance sum. On 3rd June, 2014, he has sold this house to Mr. Suri for ₹ 1,35,00,000. In the meantime on 4th April. 2015 he had purchased residential house in Delhi for ₹28,00,000. Mr. Hari has purchases another old house in Chennai on 14th October 2015, from Mr. X, an Indian resident by paying ₹ 35,00,000 and purchase was registered with the appropriate authority .

Determine the taxable capital gain arising from above transactions in the hands of Hari for assessment year 2015-16. Cost inflation index: 2005-06 = 497; 2008-09 = 582; 2013-14 939; 2014-15 = 1024; He furnished the return of Income on 31st October 2015. **(7 Marks)**

(b) Miss .C, an American national, got married to Mr. R of India in USA on 2.03.2014 and came to India for the first time on 16.03.2014. She remained in India up till 19.9.2014 and left for USA on 20.9.2014. She returned to India again on 27.03.2015. While in India, she had purchased a show room in Mumbai on 22.04.2014, which was leased out to a company on a rent of ₹ 25,000 p.m. from 1.05.2014 She had taken loan from a bank for purchase of this show room on which bank had charged interest of ₹ 97,500 up to 31.03.2015. She had received the following gifts from her relatives and friends during 1.4.2014 to 30.6.2014: - From parents of husband ₹ 51,000
- From married sister of husband ₹ 11,000
- From two very close friends of her husband, ₹1,51,000 and ₹ 21,000 ₹ 1,72,000

Determine her residential status and compute the total income chargeable to tax along with the amount of tax payable on such income for the Asst. Year 2015-16. **(8 Marks)**

3 (a) Merry home is a public charitable trust created under a trust deed for providing relief to physically challenged persons and registered u/s 12A of the Income tax Act. The following are the particulars of receipts of the tryst during the year ended 31st March 2015.

Particulars	₹ In lakhs
Income from properties held by trust (net) Income (net from business (incidental to main objects) Voluntary contribution from public (including the corpus donation ₹ 7 lakhs)	15 14 18

Thus trust applied ₹ 18 lakhs towards various activities and programme undertaken for the benefit of physically challenged persons during the year. The trust has also paid ₹8 lakhs towards repayment of a loan taken 2 years back for the purpose of construction of its centre for training the handicapped persons in various handicraft works and sports. Determine the tax liability, if any of the trust for the AY 2015-16 and also state how the trust can mitigate such liability. **(8 Marks)**

(b) S (P) Ltd gives you the following details for the accounting year ended 31.3.15.

a) Paid up equity share capital – 40,000 equity shares of 10/- each
b) A,B,C,D are registered shareholders each holding 10,000 shares.
c) The accumulated profits on 1.4.11 amounts to 40 lakhs
d) Current year profits amounts to 10 lacs.
e) Loans and advances granted during the year includes

A loan of 300,000/- given to A on 10.7.2014 out of which 100,000/- was repaid by him on 30.3.2015
Loan of 4 lakhs to B (HUF) who are the beneficial owners of the shares registered in the name of B.
Loan of 300,000 was given to M₹ C. (Given at the request of C)
Trade advance of ₹ 5,00,000 to D who supplied machine to the company. The advance was adjusted against the final payment. Discuss the tax implications of the above transactions in the hands of the shareholders and S (P) Ltd. **(7 Marks)**

4 (a) Mr. `X' furnishes the following data for the previous year ending 31.3.2015.

a) Equity Shares of AB Ltd., 10,000 in number were sold on 31.5.2014, at ₹ 500 for each share.
b) The above shares of 10,000 were acquired by `X' in the following manner :
   (i) Received as gift from his father on 1.6.1980 (5,000 shares) the market price on 1.4.81 ₹ 50 per share.
   (ii) Bonus shares received from AB Ltd. on 21.7.1984 (2,000 shares).
   (iii) Purchased on 1.2.1993 at the price of ₹ 125 per share (3,000 shares).

c) Purchased one residential house at ₹25 lakhs, on 1.9.2016 from the sale proceeds of shares.

d) `X' is already owning a residential house, even before the purchase of above house.

You are required to compute the taxable capital gain. He has no other source of income chargeable to tax. Assume exemption u/s 10(38) not available. Will your answer differ if the sale is on 1st August 2014.
(Cost Inflation Index – Financial year 1992-93: 223; Financial year 2013-2014 : 939 Financial Year 2014-2015 :1024) **(6 Marks)**

(b) From the following data you are required to work out the total income chargeable to tax and ascertain the tax thereon of S for Assessment year 2015-16. ₹

Business Loss	50,00,000
Property Income	45,00,000
Income from other sources (including Interest on PO SB 13,500)	2,13,500
Capital Gains Short Term	3,00,000
Capital Gains Long Term	10,00,000
Medical expenditure on treatment of dependent elder brother suffering from cancer	70,000
Amount deposited in PPF	1,40,000

(9 Marks)

5 (a) Mr. C inherited from his father 8 plots of land in 1980. His father had purchased the plots in 1960 for ₹ 5 lakhs. The fair market value of the plots as on 1-4-1981 was ₹ 8 lakhs. (₹ 1 lakh for each plot) On 1st June 2001, C started a business of dealer in plots and converted the 8 plots as stock-in-trade of his business. He recorded the plots in his books at ₹ 45 lakhs being the fair market value on that date. In June 2005, C sold the 8 plots for ₹ 50 lakhs. In the same year, he acquired a residential house property for ₹ 45 lakhs. He invested an amount of ₹ 5 lakhs in construction of one more floor in his house in June 2006. The house was sold by him in June 2014 for ₹ 63,50,000. The valuation adopted by the registration authorities for charge of stamp duty was ₹ 85,50,000. As per the assessee's request, the Assessing Officer made a reference to a Valuation Officer. The value determined by the Valuation Officer was ₹ 87,20,000. Brokerage of 1 % of sale consideration was paid by C. Give the tax computation for the relevant assessment yea₹ with reasoning. (CII: 1981-82 – 100; FY 2001-02 – 426; FY 2005-06 – 497; FY 2006-07 – 519; FY 2014-15 – 1024) **(7 Marks)**

(b) On 21-3-2014, Mr. T gifted to his wife Mrs. T 200 listed shares, which had been bought by him on 19-4-2013 at ? 2,000 per share. On 1.6.2014, bonus shares were allotted in the ratio of 1:1. All these shares were sold by Mrs. T as under:

Date of sale	Manner of sale	No. of shares	Net sales value (?)
21.5.2014	Sold in recognized stock exchange, STT paid	100	220,000
27. Z.2014	Private sale to an outsider	All bonus shares	1,25,000
28.2.2015	Private sale to her friend Mrs. H (Market value on this date was '2, 10,000)	100	1,75,000

Briefly state the income-tax consequences in respect of the sale of the shares by Mrs. T, showing clearly the person in whose hands the same is chargeable, the quantum and the head of income in respect of the above transactions. Detailed computation of total income is NOT required.
Net sales value represents the amount credited after all taxes, levies, brokerage, etc., and the same may be adopted for computing the capital gains. Cost inflation index for the FY 2014-15 is 1024 and for the FY20 13-14 is 939. **(8 Marks)**

PRIME ACADEMY
40TH SESSION – FINAL - PROGRESS TEST - DIRECT TAX LAWS
SUGGESTED ANSWERS
PART - A

1

a. As per Section 6 of Income Tax Act, 1961, an individual is said to be resident in India in any previous year, if he satisfies any one of the following conditions:

a. He has been in India during the previous year for a total period of 182 days or more, or
b. He has been in India during the 4 years immediately proceeding the previous year for a total period of 365 days or more and has been in India for at least 60 days in the previous year.

If an individual satisfies any one of the conditions mentioned above, he is a resident. If both the above conditions are not satisfied, the individual is a non-resident. However, the second condition is not applicable in the following cases:

1) An Indian citizen who leaves India during the previous year for the purpose of employment outside India or as a member of the crew of an Indian ship;
2) An Indian citizen or a person of Indian origin who, being outside India, comes on a visit to India during the previous year.

Conclusion:

In the given case , Mr. I was out of India for a period 200 days during 2014-15. Also, he stayed in outside India for more than 365 days for the preceding 4 years Therefore, Mr. I does not fulfills the two conditions to become a resident. Hence, Mr. I can file his income tax return or AY 2015-16 as non-resident.

Note: The problem is not clear whether Mr. I is stayed in India or outside India for a period exceeding 365 days in the preceding 4 years It is assumed that Mr. I is stayed outside India. Accordingly, problem is solved.

b. The facts of this case are similar to the facts in CIT v. Shiv Charan Mathur (2008) 306 ITR 126 (Raj.). In the instant case, the High Court observed that MPs and MLAs do not fall within the meaning of "employees". They are elected by the public, their election constituencies and it is consequent upon such election that they acquire constitutional position and are in charge of constitutional functions and obligations. The remuneration received by them, after swearing in, cannot be said to be salary within the meaning of section 15, since the basic ingredient of employer-employee relationship is missing in such cases. Therefore, the remuneration received by MPs and MLAs is taxable under the head "Income from Other Sources" and not under the head "Salaries". When the provisions of section 15 are not attracted to the remuneration received by MPs and MLAs, the provisions of section 17 also would not apply as section 17 only extends the definition of salary by providing that certain items mentioned therein would be included in salary as "perquisites". Thus, reimbursement of medical expenditure (incurred for open heart surgery abroad) to an MLA cannot be taxed as a perquisite under section 17. Applying the above ruling to the case on hand, the contention of the Assessing Officer is not correct.

c. Computation of Income from house property of Vishnu for the A.Y. 2015-16

Let us first calculate the income from each house property assuming that they are deemed to be let out.

Particulars	**In ₹**	
	House I	**House II**
Gross Annual Value (GAV)		
Expected Rent (ER) is the GAV of house property ER = Higher of Municipal value and fair rent, but restricted to standard rent	7,20,000	14,00,000
Less: Municipal taxes (paid by the owner during the previous year as a percentage of Municipal Valuation)	1,60,000	2,16,000
Net Annual Value (NAV)	**5,60,000**	**11,84,000**

Less: Deductions under section 24 (a) 30% of NAV (b) Interest on borrowed capital	 1,68,000 3,50,000	 3,55,200 5,00,000
Income from house property	**42,000**	**3,28,800**

OPTION 1 (House I – self-occupied and House II – deemed to be let out)
If House I is opted to be self-occupied, the income from house property shall be –

Particulars	₹
House I (Self-occupied) [representing interest on borrowed capital, assuming the construction of the house was completed within 3 years from the end of the financial year in which the capital was borrowed]	(2,00,000)
House II (Deemed to be let-out)	3,28,800
Income from house property	**1,28,800**

OPTION 2 (House I – deemed to be let out and House II – self-occupied)
If House II is opted to be self-occupied, the income from house property shall be –

Particulars	₹
House I (Deemed to be let-out)	42,000
House II (Self-occupied) [Loss representing interest on borrowed capital restricted to ₹ 2,00,000]	(2,00,000)
Income from house property	**(1,58,000)**

Since Option 2 is more beneficial, Vishnu should opt to treat House II as self-occupied and House I as deemed to be let out. His loss from house property would be ₹ 1,58,000 for the A.Y. 2015-16. This loss can be carried forward to the next year for set-off against income from house property of that year. It can be carried forward up to a maximum of 8 yea₹

d. Computation of long term capital gain of D for the A.Y. 2014-15

Particulars	₹	₹
Full value of consideration (Note 1)		65,00,000
Less: Indexed cost of acquisition-land (3,64,000 X1024/447) (Note 2 & 3) Indexed Cost of acquisition-building (9,60,000X 1024/ 480) (Note 3) Indexed Cost of improvement-building (5,51,000 x 1024/551)	8,33,861 20,48,000 10,24,000	 39,05,861
Long-term capital gain		25,94,139

Notes:

1. As per section 50C, where the consideration received or accruing as a result of transfer of a capital asset, being land or building or both, is less than the value adopted by the Stamp Valuation Authority, such value adopted by the Stamp Valuation Authority shall be deemed to be the full value of the consideration received or accruing as a result of such transfer. Accordingly, full value of consideration will be ₹ 65lakhs ₹ in this case
2. Since D has acquired the asset by way of gift, therefore, as per section 49(1), cost of the asset to D shall be deemed to be cost for which the previous owner acquired the asset i.e., ₹ 3,00,000, in this case.
3. Indexation benefit is available since both land and building are long-term capital assets. However, as per the definition of indexed cost of acquisition under clause (iii) of Explanation below section 48, indexation benefit for land will be available only from the previous year in which Mr. D first held the land i.e., P.Y. 2002-03.

Note: Alternative view: In the case of CIT v. Manjula J. Shah 16 Taxmann 42 (Bom.), the Bombay High court held that indexation cost of acquisition in case of gifted asset can be computed with reference to the year in which the previous owner first held the asset. As per this view, the indexation cost of acquisition of land would be ₹ 2,048,000 and long term capital gain would be ₹13,80,000

2 a) Computation of taxable capital gain of Mr. Hari for the A.Y.2015-16

Particulars	₹
Sale proceeds	1,35,00,000
Less: Indexed cost of acquisition (See Note 1)	15,32,909
Long Term Capital Gain	1,19,67,091
Less: Exemption under section 54 in respect of investment in house at Chennai(See Note 2)	35,00,000
Taxable long-term capital gain	84,67,091

Notes

1. Computation of indexed cost of acquisition

Particulars	₹
Cost of acquisition	9,94,000
Less: Advance taken and forfeited	2,50,000
Cost for the purpose of Indexation	7,44,000
Indexed cost of acquisition (₹ 7,44,000 x 1024/497)	15,32,909

Note:

1. Advance received and forfeited on or after 01.04.2014 is taxable under section 56(2)(ix). Such amount would not be reduced to compute indexed cost of acquisition while determining capital gains on sale of such property.
   However, in this case, since the advance was received and forfeited in the year 2004, such advance has to be reduced for calculating indexed cost of acquisition for the purpose of arriving at capital gains.
2. In order to avail exemption of capital gains under section 54, a new residential house should be purchased within 1 year before or 2 years after the date of transfer or constructed within a period of 3 years after the date of transfer. In this case, Hari has purchased the residential house in Delhi within one year before the date of transfer and paid the full amount as per the purchase agreement, though he does not possess any legal title till 31.3.2015 since the transfer was not registered with the registration authority. However, for the purpose of claiming exemption under section 54, holding of legal title is not necessary. If the taxpayer pays the full consideration in terms of the purchase agreement within the stipulated period, the exemption under section 54 would be available. It was so held in Balraj v. CIT(2002) 254 ITR 22 (Del.) and CIT v. Shahzada Begum (1988) 173 ITR 397 (A.P.).
3. Section 54 provides that exemption there under can be availed in respect of investment made in one residential house situated in India. It would be more beneficial for Mr. Hari to claim exemption in respect of the Chennai house since the cost of the same is higher than the cost of the Delhi house.

(b) Under section 6(1), an individual is said to be resident in India in any previous year, if he satisfies any one of the following conditions:

(i) He has been in India during the previous year for a total period of 182 days or more, or

(ii) He has been in India during the 4 years immediately preceding the previous year for a total period of 365 days or more and has been in India for at least 60 days in the previous year.

If an individual satisfies any one of the conditions mentioned above, he is a resident. If both the above conditions are not satisfied, the individual is a non-resident. Therefore, the residential status of Miss C, an American National, for A.Y.2015-16 has to be determined on the basis of her stay in India during the previous year relevant to A.Y. 2015-16 i.e. P.Y.2014-15 and in the preceding four assessment years

Her stay in India during the previous year 2014-15 and in the preceding four years are as under:
P.Y.2014-15

01.04.2014 to 19.09.2014 - 172 days
27.03.2015 to 31.03.2015 - 5 days

Total 177 days

Four preceding previous years
P.Y.2013-14 [1.4.2013 to 31.3.2014] -16 days
P.Y.2012-13 [1.4.2012 to 31.3.2013] - Nil
P.Y.2011-12 [1.4.2011 to 31.3.2012] - Nil
P.Y.2010-11 [1.4.2010 to 31.3.2011] - Nil

Total 16 days

The total stay of the assessee during the previous year in India was less than 182 days and during the four years preceding this year was for 16 days. Therefore, due to non-fulfillment of any of the two conditions for a resident, she would be treated as non-resident for the Assessment Year 2015-16.

Computation of total income of Miss C for the A.Y. 2015-16

Particulars		₹	₹
Income from house property			
Show room located in Mumbai remained on rent from 01.05.2014 to 31.03.2015 @ ₹ 25,000/- p.m.			
Gross Annual Value [25,000 x 11] (See Note 1 below)		2,75,0000	
Less: Municipal taxes		Nil	
Net Annual Value (NAV)		2,75,000	
Less: Deduction under section 24			
30% of NAV	82,500	1,80,000	
Interest on loan	97,500		95,0000
Income from other sources			
Gifts received from non-relatives is chargeable to tax as per section 56(2)(vii) if the aggregate value of such gifts exceeds ₹ 50,000.		Nil	
- ₹ 50,000 received from parents of husband would be exempt, since parents of husband fall within the definition of relatives and gifts from a relative are not chargeable to tax.		Nil	
- ₹ 11,000 received from married sister of husband is exempt, since sister-in-law falls within the definition of relative and gifts from a relative are not chargeable to tax.		1,72,000	1,72,000
			2,67,000
- Gift received from two friends of husband ₹ 1,51,000 and ₹ 21,000 aggregating to ₹ 1,72,000 is taxable under section 56(2)(vii) since the aggregate of ₹ 1,72,000 exceeds ₹ 50,000. (See Note 2 below)			

Computation of tax payable by Miss C for the A.Y. 2015-16

Particulars	₹
Tax on total income of ₹ 2,67,000	6,700
Add: Education cess@2%	134
Add : Secondary and higher education cess @1%	67
Total tax payable	6901

Notes:

1. Actual rent received has been taken as the gross annual value in the absence of other information (i.e. Municipal value, fair rental value and standard rent) in the question.
2. If the aggregate value of taxable gifts received from non-relatives exceeds ₹ 50,000 during the year, the entire amount received (i.e. the aggregate value of taxable gifts received) is taxable. Therefore, the entire amount of ₹ 1,72,000 is taxable under section 56(2)(vii).
3. Since Miss Charlie is a non-resident for the A.Y. 2015-16, rebate under section 87A would not be available to her, even though her total income is less than ₹ 5 lacs.

3 (a) Computation of total income of Merry home for AY 2015-16

Particulars	₹ In lakhs	₹ In lakhs
Income from property held under Trust (net)		15.00
Income from business (incidental to main objects)		14.00
Voluntary contribution (other than corpus)		11.00
Voluntary contribution (Corpus)	7.00	
Less: Exempt u/s 11(1)(d)	7.00	Nil
		40.00
Less: Exemption u/s 11(1)(a) 15% of Income (₹ 40 lakhs)		6.00
		34.00
Less: Exemption u/s 11(1)(a) Amount applied for charitable purpose Amount applied for repayment of loan	18.00 8.00	26.00
Total income taxable		8.00

To mitigate the tax liability, the trust can accumulate its income u/s 11(2) towards its objects by fulfilling the following conditions:

a) The trust has to give notice of accumulation in the prescribed form to the AO before the due date for filing return of income specifying therein the objects for which the income is ascertained;
b) The income can be so accumulated for a period not exceeding 5 years; and
c) The amount so accumulated should remain invested in the mode specified u/s 11(5).

(b) Any payment by a company, other than a company in which the public are substantially interested, of any sum by way of advance or loan to an equity shareholder, being a person who is the beneficial owner of shares holding not less than 10% of the voting power, is deemed as dividend under section 2(22)(e) of Income tax act, 1961, to the extent the company possesses accumulated profits.Such loan amount is considered as dividend even if the amount is repaid during the year.However, the above provision will not apply if the loan was in the normal course of business.
In the given case, each of A, B, C and D holds 10,000 shares i.e. more than 255 of the share capital. Therefore, A, B, C and D to said to have substantial interest is S(P) Limited
Accumulated profits until first day of the previous year ₹ 40,00,000.
The taxability as deemed dividend for various transactions is given below:

Loan to A:
Since A is holding substantial rights in S(P) Limited, loan advanced of ₹ 3,00,00 is treated as deemed dividend even if he repaid Rs 1,00,000.

Loan to B (HUF)
Even though on a plain reading of section 2(22)(e), it appears that the said provision would be attracted only if the person to whom the loan is given is a registered shareholder as well as beneficial owner, the Delhi High Court, in CIT v. National Travel Services (2012) 347 ITR 305/(2011) 202 Taxman 327, has

taken a view that where loan is given by a company to a firm, being the beneficial owner of shares held in the name of its partners, provisions of section 2(22)(e) would be attracted, since the essential condition to be satisfied is that of beneficial ownership and it is not necessary that the beneficial owner has to be a registered shareholder. Hence, in the loan amount of ₹ 4,00,000 given to B(HUF), who are beneficial owners of shares held by B, the loan will be treated as deemed dividend

Loan to Mr. C

Since C is holding substantial rights in S(P) Limited, loan advanced of ₹ 3,00,00 is treated as deemed dividend.

Trade advance to ₹ 5,00,000 to D

In CIT v. Rajkumar (2009) 318 ITR 462 (Del.), it was held that trade advance given to the shareholder which is in the nature of money transacted to give effect to a commercial transaction, would not be deemed to be dividend in the hands of the shareholder under section 2(22)(e). The Delhi High Court ruling in CIT v. Ambassador Travels (P) Ltd. (2009) 318 ITR 376 also supports the above view.

In the present case, the payment is made to D. for advance for supply of machinery is in the course of commercial business transaction and therefore, it shall not be deemed as dividend in the hands of Dhaval under section 2(22)(e).

4 (a) Computation of taxable capital gain of Mr. 'X' for A.Y. 2015-16

Particulars	₹	₹
Sale consideration received on sale of 10,000 shares @ ₹ 500 each Less: Indexed cost of acquisition 5,000 shares received as gift from father on 1.6.1980 Indexed cost 5,000 x ₹ 50 x 1024/100 2,000 bonus shares received from AB Ltd Bonus shares are acquired on 21.7.1985 i..e after 01.04.1981 Hence, the cost is Nil. 3000 shares purchased on 1.2.1994 @ ₹ 125 per share. The indexed cost is 3000 x 125 x 1024/244 Long term capital gain Less : Exemption under section 54F (See Note below) ₹ 8,66,230 x ₹ 25,00,000 / ₹ 50,00,000 Taxable long term capital gain		

Note: Exemption under section 54F can be availed by the assessee subject to fulfillment of the following conditions:

a. The assessee should not own more than one residential house on the date of transfer of the long term capital asset;

b. The assessee should purchase a residential house within a period of 1 year before or 2 years after the date of transfer or construct a residential house within a period of 3 years from the date of transfer of the long-term capital asset.

   In this case, the assessee has fulfilled the two conditions mentioned above. Therefore, he is entitled to exemption under section 54F.

(b) The assessee would be greatly benefited if the business loss is first set off against long tem capital gain, short term capital gains and income from other sources and only the balance is set off finally against property income so that the net amount of income taxable is other than long term capital gains. The question does not indicate the status of the assesse. Assuming that the assessee is an individual or HUF, the computation shall be as follows

Computation of total income and tax payable of 'S' for A.Y. 2015-16

Particulars	INR
Business loss Less: Long term capital gains Balance loss Less: Short term capital gains Balance loss Less: Income from other sources Balance loss Income from house property –	50,00,000 10,00,000 40,00,000 3,00,000 37,00,000 2,13,500 34,86,500 45,00,000
Gross total income	10,13,500
Less: Amount invested in PPF deduction under section 80C	1,40,000
Less: Medical expenditure on treatment of dependent elder brother suffering from cancer deduction under section 80DDB	40,000
Total taxable income	8,33,500

Computation of tax payable by S for the A.Y. 2015-16

Particulars	INR
Tax on total income of ₹8,33,500 Add: Education cess@2% Add : Secondary and higher education cess @1% Total tax payable	91,700 1,834 917 94,451

Note: Deduction under section 80DDB is restricted to 40,000 or actual amount spend whichever is less.

5 (a) Computation of total income and tax liability of Mr. C for A.Y. 2015-16

Particulars	₹	₹
Capital Gains on sale of residential house property		
Value declared by Mr. C ₹ 63,50,000		
Value adopted by Stamp Valuation Authority ₹85,50,000		
Valuation as per Valuation Officer ₹ 87,20,000		
Gross Sale consideration (See Note 1)		85,50,000
Less: Brokerage@1% of sale consideration		63,500
Net Sale consideration		84,86,500
Less: Indexed cost of acquisition (₹ 35,00,000 × 1024/497)	72,11,268	
Indexed cost of improvement (₹ 5,00,000 × 1024/519)	9,86,513	81,97,781
		2,88,719
Long-term capital gains (Total Income)		
Tax on total income (See Note 2)		
Long-term capital gain taxable@20%(₹ 2,88,719 – ₹ 2,50,000)		7,744
Less: Rebate u/s 87A		2,000
Add: Education cess @ 2%		5,744
Secondary and higher education cess @ 1%		115
Total tax liability		57
Tax liability (rounded off)		5,916
		5,920

Notes:

1. As per section 50C, in case the value of sale consideration declared by the assessee is less than the value adopted by the Stamp Valuation Authority for the purpose of charging stamp duty, then, the value adopted by the Stamp Valuation Authority shall be taken to be the full value of consideration. In case the valuation is referred to the Valuation Officer and the value determined is more than the value adopted by the Stamp Valuation Authority, the value determined by the Valuation Officer shall be ignored. Therefore, in the present case, the sale consideration would be the stamp valuation of ₹ 85,50,000,since the same is more than the sale value declared by Mr. C and less than the value determined by the Valuation Officer.

2. As per section 112, the unexhausted basic exemption limit can be exhausted against the long-term capital gains. Since Mr. C does not have any other income in the current year, the whole of the basic exemption limit of ₹ 2,50,000 is exhausted against the long-term capital gains of ₹2,88,719 and the balance long-term capital gains shall betaxable@20%. It is assumed that Mr. C is a resident individual below the age of 60yea₹

(b) Where an asset has been transferred by an individual to his spouse otherwise than foradequate consideration, the income arising from the sale of the said asset by the spouse wil lbe clubbed in the hands of the individual.Where there is any accretion to the asset transferred, income arising to the transferee from such accretion will not be clubbed. Hence, the profit from sale of bonus shares allotted to M₹T will be chargeable to tax in the hands of M₹ T.

Therefore, the capital gains arising from the sale of the original shares has to be included in the hands of Mr.T, and the capital gains arising from the sale of bonus shares would be taxable in the hands of M₹ T.

Where an asset received by way of gift has been sold, the period of holding of the previous owner should be considered for determining whether the capital gain is long term or short term. The cost to the previous owner has to be taken as the cost of acquisition.

Income/loss to be clubbed in the hands of Mr. T

Long-term capital gains/loss

	Particulars	INR
1	100 shares sold on 21.5.2014 in a recognized stock exchange, STT paid. Long-term capital gains on sale of such shares is exempt under section 10(38)	NIL
2	Shares sold to a friend on 28.2.2015 Sale consideration Less: Indexed cost of acquisition of 100 shares (₹ 2,000 x 100 x 1024/939) Long term capital loss to be included in the hands of Mr. T	 1,75,000 2,18,104 43,104

Income taxable in the hands of M₹ T

Short-term capital gains (on sale of 100 bonus shares)

Particulars	INR
Sale consideration	1,25,000
Less: Cost of acquisition of bonus shares	Nil
Short-term capital gains	1,25,000

Taxability in the hands of M₹ H under the head "Income from other sources"

M₹ Hema has received shares from her friend, M₹ T, for inadequate consideration. Even though shares fall within the definition of "property" under section 56(2)(vii), the provisions of section 56(2)(vii) would not be attracted in the hands of M₹ H, since the difference between the fair market value of shares and actual sale consideration does not exceed₹ 50,000.

PRIME ACADEMY
40TH SESSION PROGRESS TEST
INDIRECT TAX LAWS

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

PART A
Each question carries one Mark

1) Taxable event for levy of excise duty is
   a) Removal of excise goods from factory
   b) Sale of excisable goods from the place of removal
   c) Manufacture or production of excisable goods in India.
   d) All of the above

2) Who is empowered to declare a place as a warehousing station?
   a) Parliament
   b) Central Government
   c) CBEC
   d) Commissioner

3) As per section 4(3)(b) of Central Excise Act, persons shall not be deemed to be 'related', if-
   a) They are inter-connected undertakings
   b) They are associated that they have interest, directly or indirectly, in business of each other
   c) Buyer is the sole distributor of the assesses
   d) They are relatives

4) For how many years excise records, returns and documents are required to be maintained immediately after the financial year to which it pertains
   a) 8
   b) 5
   c) 3
   d) 6

5) Increase in rate of excise becomes effective
   a) Immediately unless specified otherwise
   b) After end of financial year
   c) After end of accounting year
   d) As ordered by Central Government

6) Distinction Between exempted sale and Zero rated sale is
   a) In zero rated sales, the commodity is not listed in tax schedule while in exempt sale, commodity is listed in tax schedule with Nil rate.
   b) In zero rated sales, the commodity is listed in tax schedule with Nil rate, while in exempt sale, commodity is listed in tax schedule with a rate but exemption is given by Government order.
   c) In zero rated sale, set off is available of all taxes paid on inputs , while in exempt sale, set off is not available of taxes paid on inputs.
   d) There is no distinction between zero rated sale and exempt sale

7) A visit to SSI can be done by Excise Officials subject to
   a) Written Permission of AC/DC
   b) When SSI has defaulted in payment of its dues
   c) When SSI has crossed their turnover limit
   d) No restriction on visit

8) A SSI unit manufactures a component bearing brand name of a large manufacturer. The large manufacturer uses the component in manufacture but his final product is not liable to duty. In such case
   a) SSI unit has to pay excise duty on his entire clearances
   b) SSI unit can claim exemption up to ₹ 150 lakhs and then pay excise duty on balance turnover
   c) SSI unit is not required to pay duty if the large manufacturer had given him written permission to use his brand name
   d) SSI unit is not required to pay duty if large manufacturer gives undertaking to pay duty on components manufactured by SSI.

9) If SSI Exemption scheme adopted by the assessee (manufacturer) he is not required to pay the central excise duty up to
   a) First Clearances up to ₹ 300 lacs
   b) First Clearances up to ₹ 150 lacs
   c) First Clearances up to ₹ 400 lacs
   d) First Clearances up to ₹ 100 lacs

10)
An automobile manufacturer (X) is getting a component manufactured by SSI unit (Y) as per Drawings up plied by him. Raw material and tooling required for manufacture is provided by X
   a) X is the manufacturer and duty liability is on him
   b) Y is the manufacturer and duty liability is on him
   c) X is the manufacturer but he can authorise Y to pay duty on his behalf
   d) Y is the manufacturer but duty is payable by X

11) Central Excise duty is covered under entry number….
   a) Entry No.84 and 97 of Union List I
   b) Entry No.83 of Union List I
   c) Entry No.54 of Union List I
   d) Entry No.82 of Union List I

12) The final products can be despatched directly from job worker's place if
   a) Permission of Commissioner is taken
   b) Permission of Owner of factory is taken
   c) Permission of Range Superintendent of factory is taken
   d) Permission of Additional Commissioner is taken

13) In case of criminal offences under Central Excise, Burden of proof of non existance of mens rea is on
   a) Assessee
   b) Department
   c) Court
   d) None of the above

14) Which of following items shall not be deducted from cum-duty price while computing assessable value of excisable goods for levy of duty of excise
   a) Freight charges up to depot
   b) Depot expenses
   c) Normal secondary packing-cost.
   d) Charges for processing done outside the factory after clearance

15) In excise EA-2000 audit, 'desk review' means
   a) Getting and documenting assessee's information
   b) Preparing audit plan
   c) Verification of records of assessee
   d) Reviewing findings of audit and preparing draft report

16) Cash discount is allowable as deduction from assessable value
   a) Only if given at the time of removal
   b) Allowable whether or not actually given
   c) Allowable whether given at the time of removal or even later
   d) Not allowable as deduction

17) Which one of the following will form part of transaction value?
   a) Transportation charges from the place of removal to the place of buyer
   b) Transportation charges from factory to place of removal
   c) Transportation charges from the place of distributor to the buyer
   d) Transportation charges from the place of buyer to any other place.

18) Time limit for demanding interest on duty is
   a) 1 year from relevant date
   b) 5 years from relevant date
   c) 6 months from order of AA/CEO
   d) There is no time limit

19) Education cess was levied by
   a) The Finance Act, 1994
   b) The Finance No. (2) Act, 2004
   c) Income Tax Act, 1961
   d) The Finance Act, 2006

20) Government would not like to export
   a) Goods
   b) Services
   c) Taxes
   d) None of them

21) In case excise duty is already recovered by manufacturer from customer, the refund due should be Transferred to
   a) Investor Education and Protection Fund
   b) Consumer Welfare Fund
   c) Consumer Protection Fund
   d) Consumer Education Fund

22) A Retail Sales Price of excisable goods should
   a) Include all taxes and all types of expenses
   b) Include only taxes and freight
   c) Include on freight and transport charges
   d) None of above

23) The period during which stay-order is issued by Court for issuing demand
   a) Will also be included while calculating time limit for raising demand
   b) Will not be included while calculating time limit for raising demand
   c) Will be included while calculating time limit of 1 year only
   d) Will be included while calculating time limit of 5 years only

24) Which of the following shall be included in assessable value?
   a) Damage discount
   b) Interest on delayed payment
   c) Outward handling charges after removal
   d) Storage charges within factory

25) Under the Cenvat Credit Rules, which of the following is not the mi sutilisation of Cenvat Credit
   a) Taking of CENVAT Credit without the receipt of goods specified in the document based on which credit has been taken
   b) Taking of CENVAT Credit based on invoice or document, which a person has reason to believe as not genuine
   c) Utilization of Cenvat credit of export goods in the discharge duty for goods removed for home consumption
   d) Issue of excise duty invoice without delivery of goods specified in the invoice. **(25 x 1 = 25 Marks)**

PART B **(50 Marks)**

Each question carries Five Marks

1) Determine the transaction value and the Excise Duty payable from the following information:
   Total Invoice value ₹ 1,00,000
   The invoice value is inclusive of the following:
   State Value added tax @12.50% and Octroi ₹ 2000
   Insurance from factory to Depot ₹ 1000
   Freight from factory to depot ₹ 7000
   Excise duty 12.36%

2) Compute the assessable value and Excise duty under the Central excise Act,1944, in the Following case:

Production	: 2000 units on 1.1.2014
Quantity Sold	: 450 units @200 per unit
	: 650 units@190 per unit
Sample clearances	: 50 units
Balance in Stock	: 850 units (at the end of the factory day for 1.1.2014)

   Assume that the rate per unit is inclusive of Central Excise Duty. Basic Excise duty @12% and cess as applicable.

3) Briefly discuss Exports under Bond
4) Goods cleared by EOUs into DTA- Discuss
5) Utilisation of CENVAT credit with the relevant Rule.
6) What are the entries that are to be passed for CENVAT credit on Capital goods?
7) Zuno limited is a SSI manufacturing product X. The Annual accounts for the year 2012-13 shows a gross sale turnover of ₹ 1,91,40,000, which includes excise duty and sales tax. The product attracted an excise duty rate of 12% as BED, Education cess@2%, SAH @1% and VAT @12.5%. Determine Duty liability under Notification 8/2003, if SSI had availed SSI exemption and then paid duty. On the other hand, if SSI had availed CENVAT credit on all its inputs, what would be the excise Duty liability?
8) Large Taxpayers Units- discuss.
9) Central Excise Revenue Audit- discusses.
10) Interest on Delayed payment of Duty u/s 11 AA of the Central Excise Act.

PRIME ACADEMY
40TH SESSION - FINAL - PROGRESS TEST - INDIRECT TAXES
SUGGESTED ANSWERS
PART-A

1. c) Manufacture or production of excisable goods in India.
2. c) CBEC
3. c) Buyer is the sole distributor of the assessee
4. b) 5
5. a) Immediately unless specified otherwise
6. c) In zero rated sale, set off is available of all taxes paid on inputs , while in exempt Sale set off is not available of taxes paid on inputs.
7. a) Written Permission of AC/DC
8. a) SSI unit has to pay excise duty on his entire clearances
9. b) First Clearances up to ₹ 150 lacs.
10. b) Y is the manufacturer and duty liability is on him.
11. a) Entry No.84 and 97 of Union List I.
12. a) Permission of Commissioner is taken.
13. a) Assessee
14. d)Charges for processing done outside the factory after clearance
15. a) Getting and documenting assessee's information
16. b) Allowable whether or not actually given
17. b) Transportation charges from factory to place of removal
18. d) There is no time limit
19. b) The Finance No. (2) Act, 2004
20. c) Taxes
21. b) Consumer Welfare Fund
22. a) Include all taxes and all types of expenses
23. b) Will not be included while calculating time limit for raising demand
24. d) Storage charges within factory
25. d) Utilization of Cenvat credit of export goods in the discharge duty for goods removed for home consumption

PART B

1)

	₹
Total Invoice value	1,00,000
Less: Octroi	(2,000)
Value	98,000

98,000 is inclusive of VAT and Excise Duty
Taxable turnover = ₹ 87,111(98,000*100/112.50)
Assessable Value = ₹ 77,528 (87,111*100/112.36)
Excise Duty = ₹ 9,583(77,528*12.36/100)

2)

Units	Rate per unit	Total ₹	Remarks
450	200	90000	As per Transaction value
650	190	123500	As per Transaction value
50	190	9500	Samples are valued as per Rule 4 read with rule 2(b) of Central Excise Valuation Rules, 2000.
	Assessable Value	2,23,000	

3) Exports under Bond:

A manufacturer may,

Export directly;

Or, through a merchant exporter

Where the sale is routed through a merchant exporter:

Goods can be removed with the Deemed Exporter executing a Letter of undertaking, or,

Goods can be removed with the Merchant Exporter executing a bond. Such a bond may be surety bond, or, security bond.

In either case proper invoice for export along with the packing list and ARE-1 form in quintuplicate. Four sets are to be prepared mandatorily and a quintuplicate copy (optional copy) may be prepared, if required. Such goods, can, be cleared with sealing or without sealing.

The term "sealing" means proper packing of the manufactured goods and affixing a seal thereon.

Sealing should be done by tamper proof " one time bottle seal". Ordinary lead seals should not be used. It is preferable to have sealing done at the time of removal of goods, else, it would be verified by the Customs officials at the custom station, leading to additional cost.

If the bond is executed by the Merchant Exporter, he may be required to obtain a Bank Guarantee for his banker for a specified amount. As and when he exports, he debits the running bond account with the duty payable on the export goods. When this amount equals the bond value, a fresh bond has to be executed.

If Letter of Undertaking is executed(ie manufacturer comes into picture) then a running bond may not be necessary. However, records as prescribed by the Department will have to be maintained.

Manufacturer cum exporter can export directly by furnishing LUT in Form UT 1. He need not execute a bond and is valid for 12 months. However, he may be asked to submit bond in B-1 with security or surety, if department is of the opinion that the manufacturer carries a risk/ discrepancy.

Merchant exporter can issue CT-1 form to the manufacturer based on which manufacturer can clear goods without payment of excise duty. It may be obtained from the superintendent of Central Excise upon execution of a bond.(Bond B-1).

Where the merchant exporter issues form CT-1. The ARE-1 to be signed both by the merchant exporter and the manufacturer.

4) Goods cleared by EOUs into DTA:

If a manufacturer in India procures goods from an Export oriented Undertaking(EOU) which is situated in the Free Trade Zone, the manufacturer is entitled to CENVAT credit on the duty paid by the EOU while clearing the goods. The goods manufactured and cleared by EOU to DTA are treated at par with import goods for the purposes of levying taxes.

Therefore, EOU also pay Central Excise duty but the same is equal to aggregate of duties of customs which would be leviable under the Customs Act, 1962 or any other law for the time being in force on like goods produced or manufactured outside India if imported into India if imported into India in terms of proviso to section 3(1) of the Central Excise Act,1944.Therefore, EOU pays aggregate of duty of Customs(ie {BCD + (CVD +education cess) + Edu.cess} + Spl CVD) as excise duty.

5) Rule 3: CENVAT credit

CENVAT credit allowed or may be utilised for various types of duties and taxes explained under the sub rules of Rule 3.

As per Rule 3(4) of CENVAT credit rules 2004, credit may be utilized for payment of

a) any duty of excise duty on any final products or
b) b) an amount equal to CENVAT credit taken on inputs if such inputs are removed as such or after being partially processed ,or,
c) an amount equal to the CENVAT credit taken on capital goods if such capital goods are removed as such; or

d) an amount under sub-rule(2) of rule 16 of Central Excise Rules, 2002(it means if the process to which the goods are subjected before being removed does not amount to manufacture, the manufacturer shall pay an amount equal to the CENVAT credit taken)
e) service tax on any output service.

6) Journal entry for CENVAT credit on Capital Goods

1. Capital Goods Account A/C Dr
CENVAT credit Receivable (capital goods) A/C Dr
To Party Account (or) Bank Account Cr
(Being purchase of capital goods by paying CENVAT from party vide invoice no& date)

2. PLA a/c Dr
To Bank A/c Cr
(Being the deposit of amount to designated bank in PLA a/c for payment of Excise duty)

3) Excise Duty Account a/c Dr
To CENVAT credit Receivable(capital goods) A/c Cr
To PLA A/C Cr
(Being the payment of excise duty thru utilization of CENVAT)
4) Profit and Loss account Dr
To Excise Duty Account Cr
(Being transfer of Excise Duty to Profit and Loss account)

7) i) If Zuno limited opted for the SSI exemption benefit
Up to 150 lacs, there is no excise duty, VAT will be applicable.

	₹
Gross sale turnover	1,91,40,000
Less: Exempted turnover	1,68,75,000 (1,50,00,000*112.5%)
Balance Turnover	22,65,000

Rs.22,65,000 includes the following :
Assessable value+Basic excise duty +Education cess+ Secondary and Higher Education cess+ Sales tax

	₹		₹
Assessable value	22,65,000*1/1.26405	=	17,91,859
Basic Excise duty	20,10,822*12%	=	2,15,023
Education Cess	2,15,023*2%	=	4,300
SAH Cess	2,15,023*1%	=	2,150

Therefore, the total excise duty is Rs.2,21,473

ii) if it opts for the CENVAT credit on all inputs

	₹		₹
Assessable value	1,91,40,000*1/1.26405	=	1,51,41,806
Basic Excise Duty	1,49,38,187*12%	=	18,17,017
Education Cess	18,17,017*2%	=	36,340
SAH Cess	18,17,107 *1%	=	18,170

Therefore the total excise duty is Rs.18,71,527

WN:

Assessable value	1
BED	0.12
2% CESS	0.0024
1% SAH	0.0012
	1.1236
Sales tax	0.140445
Gross Total	1.26405

8) LTU is one who meets ANY one of the following conditions:

i. Excise duty in cash(account credit) of ₹ 5 crores or more
ii. Service tax in cash(account credit) of ₹ 5 crore or more
iii. Advance(income) tax/Corporation tax of ₹ 10 Crore or more

LTUs will get facilities of payment of tax through Single window system. This means that all their tax payments, direct and indirect and all filing of returns and documents, assessments, rebates or refunds ,audit, recovery and refunds will take place at one place.

In essence, a single office would deal with central excise/service tax/income tax /corporate tax issues of all units holding a single PAN.

A LTU will be headed by a Chief Commissioner (either from CBDT or from CBEC).

9) CERA:

1. Conducted by the C&AG it is called as Central Excise Revenue Audit.
2. This is an audit of the Central Excise Department's functioning and it is carried out at the office of the Central Excise Department.
3. This is not an audit of the assessee.
4. The audit focuses on ascertaining the revenue leakage and is assessed on the basis of the periodical returns filed by the assessee, the execution of various bonds, and other relevant information such as cost audit records, and income-tax audit reports of the assessee.
5. The CERA auditor has the right to visit the office of the assessee though the audit is not of the assessee.
6. There is no defined frequency for the carrying out of this audit.
7. C&AG submits the report to the President of India, who causes these to be laid before each house of Parliament.

10) Interest on delayed payment (Section 11 AA of the Central Excise Act) should not be less than 10% and not more than 36%. The interest is payable from the next date after the due date in case of delay in payment. The interest rate is 18% pa (wef 1.4.2011).

No interest shall be payable where, the duty payable arises subsequent to the issue of an order, instruction or direction by the Board under section 37 B and such amount of duty is voluntarily paid in full within 45 days from the date of issue of such order, instruction or direction without reserving any right to appeal against the said payment at any subsequent stage of such payment.