

PRIME ACADEMY
30th SESSION - PROGRESS TEST
ADVANCED MANAGEMENT ACCOUNTING

No. of Pages: 3

Total Marks: 75

Time Allowed: 2Hrs

PART A

1. State which type of cost analysis is useful in taking managerial decisions in the following cases:
 - a. Make or Buy
 - b. Retain or Replace a machine

(2 Marks)

2. Margin of safety is the difference between _____ and _____.
 - a. Total Sales and Sales at Breakeven point.
 - b. Total Sales and Fixed Cost
 - c. Total Cost and Cost at Breakeven point.

(1 Mark)

3. Which of the following items would NOT be considered in cost-volume-profit analysis?
 - a. units of production
 - b. fixed costs
 - c. product mix
 - d. gross profit margin

(1 Mark)

4. The break-even point is
 - a. the volume of activity where all fixed costs are recovered.
 - b. where fixed costs equal total variable costs.
 - c. where total revenues equal total costs.
 - d. where total costs equal total contribution margin.

(1 Mark)

5. Which of the following equations is TRUE?
 - a. Contribution margin = Sales revenue \times Variable cost ratio
 - b. Contribution margin ratio = Contribution margin/Variable costs
 - c. Contribution margin = Fixed costs
 - d. Contribution margin ratio = 1 – Variable cost ratio

(1 Mark)

6. In 2004, A Ltd had variable costs of Rs.27,000, fixed costs of Rs.18,000, and a net loss of Rs.4,500. A Ltd's 2004 break-even sales volume was
 - a. Rs.36,000.
 - b. Rs.37,500.
 - c. Rs.49,500.
 - d. Rs.54,000.

(2 Marks)

7. Which of the following is a TRUE statement about sales mix?
 - a. Profits may decline with an increase in total Rs.s of sales if the sales mix shifts to sell more of the high contribution margin product.
 - b. Profits may decline with an increase in total Rs.s of sales if the sales mix shifts to sell more of the lower contribution margin product.

- c. Profits will remain constant with an increase in total Rs.s of sales if the total sales in units remains constant.
- d. Profits will remain constant with a decrease in total Rs.s of sales if the sales mix also remains constant. (1 Mark)
8. Which of the following is not an assumption of the Cost Volume Profit analysis.
- Changes in the level of revenues and cost arise only because of the change in the units
 - Selling price, variable cost per unit and total fixed costs within a relevant time period and range are known and constant.
 - When represented graphically, the behavior of total revenues and total cost are not linear in relation to output level within a relevant range and time period. (1 Mark)
9. The Degree of operating leverage at any given level of sales equals
- Contribution margin/Operating income
 - Operating income/Contribution margin
 - Margin of Safety*Profit Volume Ration (1 Mark)
- 10.A Relevant cost is a one
- Which differ among alternative courses of action
 - Which remains same among alternative courses of action
 - Which is Fixed across all courses of action. (1 Mark)
11. _____ is the contribution to operating income that is forgone by not using a limited resource in its next best alternative use.
- Business Function cost
 - Opportunity Cost
 - Full cost (1 Mark)
12. _____ are past costs that are unavoidable because they cannot be changed irrespective of the action taken.
- Direct Cost
 - Sunk Cost
 - Opportunity Cost. (1 Mark)
- 13.M Company projected the following information for next year:
- | | |
|------------------------------|------------|
| Selling price per unit | Rs.75.00 |
| Contribution margin per unit | Rs.30.00 |
| Total fixed costs | Rs.120,000 |
| Tax rate | 40% |
- How many units must be sold to obtain an after-tax profit of Rs.67,500?
- 3,750 units
 - 7,750 units
 - 5,625 units
 - 5,167 units (1 Mark)
- 14.D Company sells only one product at a regular price of Rs.7.50 per unit. Variable expenses are 60 percent of sales and fixed expenses are Rs.30,000. Management has decided to decrease the selling price to Rs.6.00 in hopes of increasing its volume of sales. What is the contribution margin ratio when the selling price is reduced to Rs.6 per unit?

- a. 25%
- b. 40%
- c. 75%
- d. 60%

(2 Marks)

15. On a profit-volume graph, the profit line intersects the horizontal axis at

- a. the origin.
- b. the break-even point.
- c. a volume of 1,000 units.
- d. a point where profit is greater than zero.

(1 Mark)

16. H Limited manufactures and sells two products A and B. Following are some information about A and B

	A	B
Expected sales ratio	1	3
Contribution to sales ratio	40%	50%
Total annual sales	Rs.420000	
Total Fixed Costs	Rs.120000	

The budgeted break-even sales value (rounded to nearest Rs.1000)

- a. Rs.196000
- b. Rs.200000
- c. Rs.253000
- d. Rs.255000

(3 Marks)

17. Classify the following expenses into Fixed, variable and Semi Variable

- a. Depreciation of plant and machinery
- b. Salary of managing director
- c. Telephone expenses
- d. Repairs to plant and machinery
- e. Wages of machine operators
- f. Power used in production
- g. Wages of permanent maintenance crew
- h. Factory rent.

(1/2 * 8 = 4marks)

PART – B

1. Mr. Calderone started a Pizza Restaurant in 1994. For this purpose a building was rented for Rs.400 per month. Two ladies were hired to work full time at the Restaurant and six college boys were noticed to work 30 hours per week delivering pizza. An outside accountant was hired and Tax and Book keeping purposes. For this service, Mr. Calderone pays Rs.300 per month. The necessary restaurant equipment and delivery van were purchased with cash. Mr. Calderone has noticed that expenses for utilities and supplies have been rather constant.

Mr. Calderone increased his business between 1994 and 1997. Profit has more than doubled since 1994. Mr Calderone does not understand why his profits have increased faster than his volume.

A Projected income statement for 1998 has been prepared by the accountant and is shown below:

**Calderone Co. projected Income statement
For the year ended Dec. 31, 1998**

	Rs.	Rs.
Sales (@ Rs. 2.50 per pizza)		100000
Cost of food sold	30000	
Wages & Fringe benefits of Restaurant Help	8150	
Wages & Fringe benefits of Delivery boys	17300	
Rent	4800	
Accounting services	3600	
Depreciation of delivery man	4000	
Depreciation of Restaurant equipment	3000	
Utilities	2450	
Supplies (Soap, Floor wax etc.)	2200	
		75500
Net Income before Taxes		24500
Income Taxes (@ 30%)		7350
Net Income after Tax		17150

Required:

1. What is the Break even point in number of pizzas that must be sold?
 2. What is the cash flow break even point?
 3. If Mr. C. withdraws Rs.4,800 for his drawing what is the net cash inflow?
 4. What should be the volume to get an after tax net income of Rs. 19,600/-
 5. Briefly explain as to why the cash flow for 1998 exceeds the profit.
 6. Analyze as to why the rate of increase in profits is more than the rate of increase in sales.
- (15 MARKS)

2. The mount hospital is unionized. In 19X3 nurses received an average annual salary of Rs.40000. The hospital administrator is considering how the contract with nurses should be changed. In turn, the charging of nursing costs to each Department is accountable for its financial performance. Revenues and expenses are allocated

to departments. During 19X3 the obstetrics department has a capacity of 60 beds, billed each patient an average of Rs.500/- per day, and had revenues of Rs. 8 million.

The expenses of the obstetrics department in 19X3: (Rs. 000s)

Variable expenses (based on 19X3 patient days)	Rs.	Fixed expenses (based on number of beds)	Rs.
Meals	320	Rent	2000
Laundry	100	General Administration services	1500
Laboratory	700	Monitorial	100
Pharmacy	400	Maintenance	200
Maintenance & Other	80	Other	200
Total	1600	Total	4000

Nurses are assigned to departments on the basis of annual patient days. The obstetrics dept. always employs only the minimum no. of nurses. Hence the salaries of nurses within the ranges of patient-days mentioned below are always fixed.

Volume level in patient days	No. of nurses
9,000 - 14,000	35
14,001 - 17,000	55
17,001 - 19,500	75
19,501 - 21,900	85

Required:

1. Compute the 19X3 patient days that would have been necessary for the Obstetrics department to break even.
2. Compute 19X3 patient days that would have been necessary to earn an operating income of Rs. 5 lakhs.
3. If obstetrics Dept. decides to pay Rs.150 per patient day for nursing services instead of the four level fixed cost system employed in 19X3. What would be your advice?

(15 Marks)

3. Lee electronics manufactures four types of electronic products, A, B, C and D. All these products have a good demand in the market. The following figures are given to you:

	A	B	C	D
Material Cost (Rs/u)	64	72	45	56
Machining Cost (Rs/u) @ Rs. 8 per hour	48	32	64	24
Other Variable Costs (Rs/u)	32	36	44	20
Selling Price (Rs/u)	162	156	173	118
Market Demand (units)	52,000	48,500	26,500	30,000

Fixed Overheads at different levels of operation are:

Level of operation (in production hours)	Total Fixed Costs (Rs)
Up to 1,50,000	10,00,000
1,50,000 – 3,00,000	10,50,000
3,00,001 – 4,50,000	11,00,000
4,50,001 – 6,00,000	11,50,000

At present, the available production capacity in the company is 4,98,000 machine hours. This capacity is not enough to meet the entire market demand and hence the production manager wants to increase the capacity. The company wants to retain the customers by meeting their demands through alternative ways. One alternative is to sub-contract a part of its production. The sub-contract offer received is as under:

	A	B	C	D
Sub-Contract Price (Rs/u)	146	126	155	108

The company seeks your advice in terms of products and quantities to be produced and/or sub-contracted, so as to achieve the maximum possible profit. You are required to also compute the profit expected from your suggestion.

(20 MARKS)

PRIME ACADEMY
30th SESSION– PROGRESS TEST
FINAL - ADVANCED MANAGEMENT ACCOUNTING
SUGGESTED ANSWERS

Part – A

1. a. Marginal Cost analysis
b. Total Differential cost analysis

Question No.	Answer
2	a
3	d
4	c
5	d
6	d
7	b
8	c
9	a
10	a
11	b
12	b
13	b
14	a
15	b
16	c

17.

- a) Semi-Variable
- b) Fixed
- c) Semi-Variable
- d) Semi-Variable
- e) Variable
- f) Variable
- g) Fixed
- h) Fixed

Part – B

1.		Rs.
	Selling price per pizza	2.50
	Variable cost (Cost of food sold)	0.75
	Contribution per pizza	1.75
	Fixed Costs	45,500
	Break Even point (no of pizza's)	26,000

	Cash Break Even	
	Fixed Costs	45,500
	– Depreciation	7,000
	Cash Fixed Costs	38,500
	Cash Break Even point (no of pizza's)	22,000

	Net Cash Inflow	
		Rs
	Profit after tax	17,150
	Add : Depreciation	7,000
	Less : Drawings	(4,800)
	Net Cash Inflow	19,350

Volume to get an after tax net income of Rs. 19,600

	After tax Desired profit	19,600
	Pre Tax Desired profit	28,000
	Add: Fixed Costs	45,500
	Total	73,500
	No of Pizza's to be sold	42,000

2.

	Rs.	Rs.	Rs.	Rs.
Range	9000-14000	14001-17000	17001-19500	19501-21900
Total Fixed Cost				
General Cost	4,000,000	4,000,000	4,000,000	4,000,000
Salary of nurses	1,400,000	2,200,000	3,000,000	3,400,000
	5,400,000	6,200,000	7,000,000	7,400,000
Contribution per patient day	400	400	400	400
Break-even patient days	13,500	15,500	17,500	18,500#
# Not a break-even since it is outside the range				
No of days required to earn a income of Rs.5,00,000				
Total Fixed Costs	5,400,000	6,200,000	7,000,000	7,400,000
Profit Desired	500,000	500,000	500,000	500,000
TOTAL	5,900,000	6,700,000	7,500,000	7,900,000
Contribution per patient day	400	400	400	400
Break-even patient days	14,750	16,750	18,750	19,750
	Not within the range			
Total Fixed Costs	4,000,000			
Contribution per patient day	250			
Break-even patient days	16,000			

3.

	A Rs.	B Rs.	C Rs.	D Rs.
Selling price	162	156	173	118
Material cost	64	72	45	56
Matching cost	48	32	64	24
Other variable costs	32	36	44	20
Total cost	144	140	153	100
Sub-contract cost	146	126	155	108
Savings on manufacture	2	-14	2	8
Decision	Manufacture	Sub-contract	Manufacture	Manufacture

	A	B	C	D	TOTAL
Contribution/unit	18		20	18	
Contribution/unit-SC	16	30	18	10	
Machine hours/unit	6	0	8	3	
Contribution/machine hour	3	0	2.5	6	
Ranking	2		3	1	
Demand(units)	52000	48500	26500	30000	
Hours reqd	312000	0	212000	90000	
Allocation of 498000hrs	312000		96000	90000	498000
Units produced	52000		12000	30000	
Units purchased		48500	14500		
Contribution-prodn	936000		240000	540000	
Contbn purchased		1455000	261000	0	
Total contbn	936000	1455000	501000	540000	3432000
Less: fixed cost					1150000
PROFIT					2282000

	A	B	C	D	TOTAL
Alternative 1	312000		48000	90000	450000
Units produced	52000		6000	30000	
Units purchased		48500	20500		
Contribution-production	936000	0	120000	540000	
Contribution purchased	0	1455000	369000	0	
Total contribution	936000	1455000	489000	540000	3420000
Fixed cost					1100000
Profit					232000
Difference in profit					38000
Alternative 2	210000			90000	300000
Units produced	35000			30000	
Units purchased	17000	48500	26500		
Contribution-production	630000	0	0	540000	
Contribution purchased	272000	1455000	477000	0	
Total contribution	902000	1455000	477000	540000	3374000
Fixed cost					1050000
Profit					2324000
Difference in profit					42000

PRIME ACADEMY
30th SESSION PROGRESS TEST
INFORMATION SYSTEMS CONTROL AND AUDIT

No. of Pages: 2

Total Marks: 75

Time Allowed: 2Hrs

25 Marks

PART-A

1. Stage three of SDLC is called as _____
2. An application programmer is involved in the _____ stage of SDLC
3. If software base lining is absent it increases the risk of _____
4. A usable system or a system component built quickly at a lesser cost and with the intention of being modified or replaced with a fully operational system is called as _____
5. In the “Bottom up” approach to systems development the first step is identification of _____
6. Estimation by the design team of the time involved for making the new system functional is part of _____ feasibility study.
7. The expansion of the term CASE is _____
8. “Data about Data” is called as _____
9. The characteristic of the codes which provide for future growth is called as _____
10. _____ is the deliverable of the design phase which is a document containing description of the activities carried out with diagrammatic representations like flow charts.
11. _____ refers to the capability to alter the system to meet the changing business requirements.
12. _____ is a method of checking the system using the documents/inputs available without using the system for testing.
13. Which of the following is not a conversion strategy:
i. Gradual Conversion ii. Debugging iii. Direct change over
14. By implementing controls, management ensures that _____ objectives are achieved and _____ events are avoided.
(2 Marks)
15. The two impacts of implementing controls are _____ and _____
(2 Marks)

16. Integrity and competency of personnel, segregation of duties, maker-checker concepts are examples of _____
17. Correct input and wrong processing will always lead to wrong output. This is termed as _____ error.
18. Review of audit logs is an example of _____ control
19. Controls which replace a similar control is called as _____ and controls which reduce the risk of primary control not being there is called as _____
(2 Marks)
20. A methodology of testing the software component's operating effectiveness without regard to any specific internal program structure is called as _____
21. Initial set of test case, which are usually very comprehensive are called as _____
22. A methodology wherein a set of fictitious records are placed in master file and processing along with record records are called as _____

PART B

50 Marks

Q. No.1 is compulsory. Answer **any 2** from the remaining 3 questions

- 1 (a) Describe six stages of SDLC in brief (10 Marks)
(b) There are many reasons why Organisations fail to meet systems development objective- Explain (6 Marks)
- 2 (a) “The move towards more automated financial statements has had an impact in the way auditors carry out their work”- explain (10 Marks)
(b) What are audit trails ? Explain the objectives of audit trails ? (7 Marks)
- 3(a) Define the concepts of identification, authentication and authorization. Explain the approaches to authentication and authorization (10 Marks)
(b) What are the causes for errors and bugs in softwares? (7 Marks)
4. Write Short Notes on :
- a. Packet Filtering Firewall (5 Marks)
 - b. Crypto systems (5 Marks)
 - c. Unit Test Plan (4 Marks)
 - d. Static Testing (3 Marks)

PRIME ACADEMY
30th SESSION- PROGRESS TEST
INFORMATION SYSTEM CONTROL AND AUDIT
SUGGESTED ANSWERS

PART – A

Q.NO.	Answer
1	Systems Design
2	Stage4 or development stage
3	Scope Creep
4	Prototype
5	Life Stream Systems
6	Schedule Feasibility
7	Computer Aided Software Engineering
8	Meta Data
9	Expandability
10	Systems Manual
11	Maintainability
12	Desk Checking/Paper Walk Through
13	ii. Debugging
14	Business objectives are achieved and undesired events are prevented
15	i. Involves cost and ii. May slow down business processes
16	Preventive Control
17	Systematic
18	Detective Control
19	i. Alternate Controls ii Compensating Controls
20	Black box testing
21	Base Case
22	Integrated Test Facility (ITF)

PART B

1)

a) Stage 1: Preliminary investigation:

- **When undertaken:** Preliminary investigation is undertaken when users come across a problem or an opportunity and submit a formal request for a new system to the MIS department.
- **Steps involved :** Preliminary investigation consists of three broad steps
 1. **Request clarification:** Requests submitted by the users may require some clarification before system investigation can commence. This is to determine as to what the user actually wants.
 2. **Feasibility study:** The system analyst carries out technical, financial, operational, schedule and legal feasibility study to determine whether the proposed system is feasible or not.
 3. **Approval of the request:** Some requests may get eliminated at the feasibility study stage. Based on the analyst's observations, the management decides which system should be taken up for development. Approval is critical as management commits resources (capital, manpower) at this stage.

Stage 2: Requirement Analysis or Systems Analysis:

- Once the management decides to go ahead with the development, the user needs should be studied in detail.
- The systems analyst uses various tools like interviews, questionnaires, environment analysis to understand the requirements.
- He identifies the problems and short comings of the existing system which should be addressed in the new system

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

- The user requirements as identified are incorporated in the design of the new system.
- In this stage various reports, outputs, inputs, files are designed to show how user requirements will be met.

- The detailed design is then given to the programmers so that they can start the development (i.e. coding/programming).
(Similar to how the architect's plans are given to the construction contractor to start construction activity)

Stage 4: Development and Acquisition of software:

- After resolving the design details, resources needed like hardware, software are determined.
- The organisation may decide buy or lease or to develop the software in-house
- If the software is to be developed in-house, the analyst works closely with the programmers and also works in the documentation of the software and the procedure manuals.

Stage 5: Systems Testing:

- Before information system can be introduced in live/production environment, it needs to be tested to ensure that software does not fail and that it runs according to specifications given by the users.
- Set of test data (called as test cases) are fed into the new system and the results examined with the expected results. Afterwards the new system may be fed with sample live data and results examined.

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

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

Stage 6: Implementation and Maintenance:

- After a system passes through the testing process, it is implemented in live area.
- New hardware if required is installed and users are trained to work on the new system.
- After the system has stabilised in live area, it is monitored to ensure that it satisfies user requirements.
- It may also undergo some maintenance efforts to adapt to changing user and business needs.

b)

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 organisation 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.

Example: When computerization was 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 as effective as the user who uses it.

2)

- a) As organisations move towards computerisation of their business processes (Information Systems), the internal control mechanisms and audit processes also undergo a change. While the control objectives (purpose to be achieved by implementing a control) in an computerised environment may remain same as in manual environment, the manner in which controls are implement may be different.

For example internal controls as known in manual environment (i.e non computerised environment) like physical verification of documents or two people authorising high value payments by signing the vouchers etc. may not work in a computerised environment. These may be replaced by online authorisation process etc.

The impact of IS on audit process can be classified into:

1. Change in audit trail and audit evidence (i.e moving towards digital evidence)
2. Change in internal control environment
3. High probability for unconventional errors and frauds (i.e cyber crimes)
4. Change in audit procedures

1. Change in audit trail and audit evidence

While in manual environment audit trails were easily visible and traceable, in computerized environment the audit trails are fragmented and difficult to trace. For example a payment voucher manually generated provides sufficient audit trail. If the same payment is made through say electronic clearing system or net banking, audit trails are not very visible and difficult for the auditor to trace. This is called as digital evidence. Issues relating to digital evidence are:

- a. Data Retention Policy: Depending on the data retention policy of and organisation, past transactions may or may not be readily available for verification on the system. They may have to be retrieved on demand. Also the data stored on the system may require specific software to interpret the data and may be as easy as auditing from a printed document.

b. Direct data entry or lack of physical input documents: Many transaction processing systems work under the direct entry mode wherein data is input into the system directly without any supporting documents- for example ATM transactions which affects account balances but has no input documents.

c. Lack of visible audit trail or short retention period of audit trails: Some organisations retain audit trails only for a short period of time- thus auditors may have to modify his audit approach suitably to look for compensating controls

d. Reduction in printed outputs : As printed outputs are declining, audits may have to be carried out directly on data on the system through a separate access mechanism.

e. Automated or system generated transactions: Certain transactions are system generated- for example if safety stock and re-order limits are set in an ERP, on reaching a particular stocking quantity, the ERP system may generate an automated purchase order and even email it to the supplier/vendor. Such transactions have no human intervention for authorisation and hence no judgement thereby increasing the chances of errors.

f. Legal Issues: In contracts and payments which are concluded online, territorial jurisdiction issues arise as regards place of origination, taxation, dispute resolution etc. For example for an online purchase of goods, the buyer may be located in one state, the web site may be located in a server in another state or country, the goods may be shipped from a different location and payment may be credited online with a Bank in another country. In such a transaction, fixing the jurisdiction for say a dispute is quite difficult.

Similarly admissibility of digital evidence-i.e whether it is good evidence or not- in a court of law is a challenge and is in very nascent stages.

2. Change in internal control environment

Some of the basic internal controls in an organization pertain to:

- Integrity and competency of personnel
- Segregation of duties in order to ensure that a single person cannot put through a transaction end to end.
- Maker-checker or authorization procedures
- Control over documents
- Access restrictions over assets and records (ex: cash as an asset can be accessed only by authorized personnel)
- Overall control and supervision by the management

While the need for the above mentioned controls are there even in a computerized environment, the methodology of implementing the controls may be different. For example:

a. Segregation of duties: In manual environment the auditor was concerned with say whether the maintenance of cash function was segregated from the physical verification of cash function. Similar control in computerized environment would be segregation within IT Department- say systems administration function should be segregated from computer operator function.

In computerized environment proper segregation of duties is essential since a risk arises if one employee or group of employees are aware of the complete data flow and process logic.

b. Centralization of data and application programs: Predominantly most organizations choose to centralize their data and programs in a single server or servers in one location. For example all the program and customer data of a Bank is located in one location called as the Data Centre. This is in contrast to a manual environment where data was stored in distributed locations (say at various branches). While centralization helps in operational efficiency, the impact of a

threat is far greater since there is concentration at one place. For example if the data centre fails or is hacked, entire operations would come to a stand still.

c. Access Controls: While in manual environment access control was predominantly physical access control (like door locks, security guard etc.) in computerized environment the access controls are predominantly logical access controls (like passwords, PIN etc.).

3. High probability for unconventional errors and frauds (i.e cyber crimes)

a. Triggered transactions or system generated transactions: As discussed in earlier paragraphs, system generated transactions are difficult to trace and audit and it requires knowledge about the program functioning.

b. Systematic errors : Computers are programmed to do transactions in a consistent manner- i.e same inputs with the same application software would generate same outputs every time. Thus correct input and correct processing would always lead to correct output. While correct input with wrong processing would always lead to wrong output. For example one error in payroll software can lead to all net salary values for the month being calculated erroneously. Thus the impact is wide spread and needs to be corrected at the source rather than at the transaction level.

4. Change in audit procedures

Since most of the audit evidence required to form an opinion is system based, manual audit procedures may not prove to be effective in a computerised environment. For example use of audit tools like ACL, IDEA may be required to query data and obtain sufficient evidence from a computerised environment.

b) Meaning: It refers to recording or logging of activities at the operating system, network, application software, user and database levels. For example application logs contain details of who initiated a transaction, who authorised it, date and time etc.

S.No.	Objective	Example
a.	Help detect unauthorised access or attempted access to the system	An unauthorised user trying a user-id password wrong three times would be logged by the system
b.	Facilitate reconstruction of events in case of system failure	Database logs contain before image and after image of data values which help reconstruct the database tables in case of a failure.
c.	Fixing of accountability	transactions can be traced to individual users based on the user-id details appearing in the logs. The person carrying out the transaction cannot later deny it since his user-id is captured in the log.

Explanation for the objectives:

a. Detecting unauthorised action: This detection can be either real time detection or after the fact detection. Real time detections are alerts configured to trigger even when unauthorised access is being attempted. These are very effective but require a lot of processing resources and monitoring mechanisms. The other alternate is to store the logs and review it as and when required.

b. Facilitate reconstruction of events: Logs keep track of events leading to system failures, security violations and application processing errors (ex: errors in calculation of interest and charges). These logs help analyse the error condition and prevent future occurrence. Similarly logs help reconstruct account balances if the files are corrupted.

c. Fixing accountability: Using logs user activity can be monitored and this acts as a deterrent against unauthorised access or policy violations by users.

3)

a) Access Controls mechanisms follow three broad steps :

Step 1: **Identify the user** – in this step the user identifies himself to the system by typing in say his user-id. He may also type-in a password.

Step 2: **Authenticate** – the system authenticates the user by comparing the password or authentication credentials provided with what is previously stored (say in an access list)

Step 3: **Authorisation** – once authenticated, the specific resources which the user can access and what privileges he has (say read, write, modify, delete etc.) is enabled.

1. What one remembers : like name, user id, passwords, PIN etc
2. What one has (possesses): like badge, plastic card, smart card, key etc.
3. What one is (physiological traits) : called as bio-metrics- like finger print, voice print, palm scan, retina scan, hand-geometry etc.
4. Dialog: Through/around the computer

b)

i. Errors associated with specifications/ requirements:

Specifications form the basis for software development. Following conditions associated with specifications give rise to errors:

- a. Specifications are not documented
- b. Specifications are not comprehensive
- c. Constant change in specifications (shift in baseline/requirements)-lack of proper communication to the development team

ii. Errors associated with design:

Design is the stage wherein the specifications are converted into a format understood by programmers. Following conditions associated with design give rise to errors:

- a. Improper design
- b. Constant change in design
- c. Improper/lack of communication

iii. Errors associated with programming (i.e writing of codes)

These are errors which creep in while the programmer is involved in the coding- i.e converting the design into a software program by writing lines of codes/instructions.

Following conditions associated with design give rise to errors:

- a. Complexity of the program logic
- b. Lack of or poor documentation
- c. Time and cost pressures associated with delivery schedules (i.e need to deliver the software within a short span of time due to cost, time or business pressures)
- d. Programmers quality

Programming errors may be traced to poor specifications or poor testing processes.

4) a. Packet filtering firewall:-

Router packet filtering firewall: Has a filtering/screening router which has to be programmed with the filtering rules. It implies that the router should be told which packet from which source IP address should be allowed to which destination IP address - Based on the rules accepts or denies access

They provide low cost, low security access control

Disadvantages:

- i. Designed for free flow of information, rather than to restrict it . No explicit authentication of outside users takes place and does not examine packet contents
- ii. Vulnerable to IP spoofing attacks where hackers disguise packets as originating from authorised users and gain access to network.

b. Public key encryption

Meaning: Uses **two different keys – one for encryption and other for decryption of the message.**

Each recipient has a public key which is published and a private key which is kept secret. Sender encrypts the message using the receiver's public key and then transmits the message. Receiver decrypts the message using his private key .

Advantage : User need not share his private key and hence reduces chances of misuse

Limitation: It may be a costly method compared to private key encryption.

- c. **a. Unit Test Plan:** These plans detail how individual units (specific portions of the software) are to be tested. UTP normally tests the basic input and output of the units along with basic functionality. It would also address the flow or sequence of testing- for example whether to test extreme values (which system should ideally reject) first or to test normal (which system should normally process) values first, the priority of the test cases and their grouping etc.

Unit test plan tests independent units as such- interface between the units is scoped out of the unit test plan. (Addressed as part of integration test plan). It also lists the tools to be used for testing, the order of priority of various software units to be tested, standardization or naming convention for test cases, reporting and re-testing approach etc.

d. Static Testing

Software testing is broadly classified as static testing and dynamic testing. **Static testing** is basically desk checking or walk-through where work is mapped to a pre-determined standard or a check-list. Can be used for say reviewing coding against coding standards. Static testing *does not* involve any input or output operations.

PRIME ACADEMY
30th SESSION - PROGRESS TEST
DIRECT TAX LAWS

No.of.page: 1

Total Marks: 75
Time Allowed: 2Hrs

PART – A

25 Marks

State whether the following statements are True or False

1. Any income derived from saplings or seedlings grown in a nursery shall be deemed to be income from Profits and Gains of Business or Profession
2. The amount of tax payable shall be rounded off to the nearest multiple of ten.
3. If the diversion of income is at source by over riding the title then such income cannot be taxed in the hands of the assessee.
4. Gross Total Income is the income arrived at after allowing deduction under chapter VI A
5. Under certain provisions of the Income Tax Act the income of the previous year is taxed in that year itself.
6. Income received, or accrued, or arising in India shall be taxed in India irrespective of the residential status of the assessee.
7. For a Firm or AOP the control and management should be wholly situated in India for it to be a resident.
8. A work of Art though a personal effect is a Capital Asset
9. The period of holding in the case of financial assets shall be reckoned from the date of subscription of such assets.
10. The cost of acquisition of an asset acquired by way of gift is NIL
11. If the minor child is suffering from a disability as specified in section 80U, then the income of such child is not clubbed.
12. Unexplained expenditure treated as income under section 69C, is not allowed as a deduction under any head of income.
13. Inter source adjustment is not allowed for Long Term Capital Gains
14. In a business reorganization of co-operative banks the losses of the predecessor is allowed to be setoff and carried forward for 8 assessment years.
15. Losses under the head Income from House Property cannot be carried forward unless the return of income is filed in accordance with the provisions of section 139(3)

(15 X 1 = 15 Marks)

Answer in couple of sentences

1. Definition of “Previous Year”
2. Definition of “Interest”
3. Define “Income Deemed to be received”
4. Define “Fair Market Value”
5. Define “Transfer”

(5 X 2 = 10 Marks)

PART – B**50 Marks**

1. Mr.Vijay submitted the following information relevant for the previous year ending on March 31st 2010

Particulars	Amount – Rs.
Profit of business carried on in India	90,000
Loss of business B carried on India	(-) 30,000
Profits of Business C carried on in Tokyo (income is earned and received in Tokyo and business is controlled from Tokyo)	52,000
Loss of business D carried on in Tokyo (Though the profits are not received in India the business is controlled from Chennai)	(-) 46,000
Unabsorbed depreciation of business D	63,000
Income from property situated in India	22,000
Income from property situated in Singapore (received in Singapore)	1,92,000

Determine the income of Mr.Vijay for the assessment year 2010-11 on the assumption that he is (a) resident and ordinarily resident in India (b) Resident but not ordinarily resident in India (c) Non-resident in India.

(9 Marks)

2. Write short notes on any two of the following

- (i) Section 10BA Special Provisions in respect of export of certain articles or things
(ii) Section 47A – Withdrawal of exemption

(5 X 2 = 10 Marks)

3. Discuss

- (i) Explanation 1 to section 32(1) provides for depreciation on building not owned by the assessee but in respect of which the assessee holds a lease or other rights of occupancy. What is the meaning of “Other Rights” in this context and will this include tenancy rights?
- (ii) The assessee has inherited a property from his father during the previous year 2002-03. The property was originally acquired by assessee’s father in the previous year 1993-04. Is the assessee right in claiming that he would index the cost from 1993-04 at the time of sale?

(3 X 2 = 6 Marks)

4. What is meant by “Reverse Mortgage”? Discuss the tax implications of a transaction of reverse mortgage.

(5 Marks)

5. X purchases 4,000 equity shares in Y Ltd. on April 16, 1985 at the rate of Rs. 2 per share. Y Ltd. goes into liquidation on June 30, 2009. The balance sheet of the company as on June 30, 2009 is as follows-

	Rs.		Rs.
40,000 equity shares	4,00,000	10,000 Debentures of Z Ltd. (cost: Rs. 9,00,000, acquired in May 2005)	28,00,000
Accumulated profit	30,00,000	Cash in hand	11,09,850
Provision for dividend tax	5,09,850		
	----- 39,09,850 =====		----- 39,09,850 =====

The assets are distributed to the shareholders. Consequently, X gets 1,000 debentures of Z Ltd. (market value Rs. 2, 80,000) and Rs. 60,000 in cash on June 30, 2009. He transfers 1,000 debentures on April 6, 2010 for Rs. 3, 10,000. Find out the tax consequences of these transactions.

(8 Marks)

6. What is the tax treatment in respect of anonymous donations received by the following trusts during the financial year 2009-10?

- (i) A charitable trust referred to in section 11 which applied the entire amount of anonymous donations for purposes of the trust during the financial year 2009-10
- (ii) A trust established wholly for religious purposes which applied 85% of the amount of anonymous donations for the purposes of the objects of the trust during the financial year 2009-10.

(3 X 2 = 6 Marks)

7. "The illegality tainted with the income has no bearing on its taxability" – Elucidate this statement with the help of a recent case law.

(3 Marks)

8. Sri Sajjan converted the capital asset, acquired by him in the year 1988, into stock-in-trade at the fair market value on 1st March, 2008. Sri Sajjan sold the entire stock-in-trade so converted, on 25th November, 2009. Sri Sajjan seeks your advice as to the tax implications of the transaction with reference to the provisions of Indian Income-tax Act for the assessment year 2010-11.

(3 Marks)

PRIME ACADEMY
30th SESSION-PROGRESS TEST
FINAL – DIRECT TAX LAWS
SUGGESTED ANSWERS

Part – A

1. False
2. True
3. True
4. False
5. True
6. True
7. False
8. True
9. False
10. False
11. True
12. True
13. True
14. False
15. False

1. Previous Year

Means the financial year immediately proceeding the assessment year

2. Interest

Interest means interest payable in any manner in respect of any moneys borrowed or debt incurred (including a deposit, claim or other similar right or obligation) and includes any service fee or other charge in respect of the moneys borrowed or debt incurred or in respect of any credit facility which has not been utilized

3. Fair market value,

In relation to a capital asset, means

(i) The price that the capital asset would ordinarily fetch on sale in the open market on the relevant date; and

(ii) Where the price referred to in sub-clause (i) is not ascertainable, such price as may be determined in accordance with the rules made under this Act

4. Transfer

Transfer, in relation to a capital asset, includes,

- i.** The sale, exchange or relinquishment of the asset; or
- ii.** The extinguishment of any rights therein; or
- iii.** The compulsory acquisition thereof under any law; or
- iv.** In a case where the asset is converted by the owner thereof into, or is treated by him as, stock-in-trade of a business carried on by him, such conversion or treatment;]

[or]

(iva) the maturity or redemption of a zero coupon bond; or

(v) any transaction involving the allowing of the possession of any immovable property to be taken or retained in part performance of a contract of the nature referred to in section 53A of the Transfer of Property Act, 1882 (4 of 1882) ; or

(vi) any transaction (whether by way of becoming a member of, or acquiring shares in, a co-operative society, company or other association of persons or by way of any agreement or any arrangement or in any other manner whatsoever) which has the effect of transferring, or enabling the enjoyment of, any immovable property.

Part B

1.

Particulars	Resident and ordinarily resident Rs.	Resident but not ordinarily resident Rs.	Non-resident Rs.
Business Income			
Business A	90,000	90,000	90,000
Business B	(-) 30,000	(-) 30,000	(-) 30,000
Business C – Note 1	52,000	Nil	Nil
Business D – Note 2	(-) 46,000	(-) 46,000	Nil
Unabsorbed depreciation of Business D – Note 2	(-) 63,000	(-) 63,000	Nil
Business Income/Loss	3000	(-) 49,000	60,000
Income from property situated in India	22,000	22,000	22,000
Income from property situated in Singapore	1,92,000	Nil	Nil
Gross Total Income	2,17,000	(-) 27,000	82,000
Less : Deduction under chapter VIA	Nil	Nil	Nil
Total Income	2,17,000	(-) 27,000**	82,000

Note 1 – U/s.5 of the Income Tax Act incidence of tax depends on the both the residential status as well as the place and time of the accrual or receipt of the income. In the given case the income from business C is earned and received in Tokyo and the business is also controlled from Tokyo. Hence the income is taxable only in the case of resident and ordinarily resident in India

Note 2 – The income not received in India though the business is controlled from India is not taxable in the hands of non-resident. Hence any loss arising from such business is also not allowed to be set-off. Similar treatment is applicable for unabsorbed depreciation also.

** The loss of Rs.27, 000 will be carried forward

2.

a) Section 10BA

Nature and Period of Deductions

Deduction is available in respect of Profits and Gains derived by the assessee from such Industrial Undertaking. No deduction however can be claimed under this section beyond the assessment year 2009-2010

Quantum of Deduction

Profits derived by the undertaking x Export Turnover of the undertaking / Total Turnover of the undertaking

Conditions Prescribed

The Industrial Undertaking to be eligible for deduction under sections 10A and 10B should satisfy the following conditions

1. It should not be formed by splitting up or the reconstruction of a business already in existence.
2. It should not be formed by the transfer to a new business of machinery or plant previously used for any purpose. The value of machinery or plant previously used for any purpose can however be upto 20% of the total value of machinery or plant of the undertaking. Machinery or plant used outside India on which depreciation has not been claimed in India will not be treated as machinery or plant previously used.
3. It manufactures or produces article or thing without the use of imported raw material
4. 90% or more of the sales is by way of export of the eligible articles or things.
5. It employs 20 or more workers during the previous year in the process of manufacture or production
6. The undertaking does not claim deduction under sections 10A or 10B

General

1. The sale proceeds of articles or things exported out of India should be received in or brought into India by the assessee in convertible foreign exchange within a period of 6 months from the end of the previous year or within such further periods as the competent authority may allow in this behalf.
2. The deduction under section 10BA shall be admissible only if the assessee furnishes along with the return of income a report in a prescribed form given by a Chartered Accountant certifying that the deduction has been claimed correctly.
3. Export turnover means the amount brought into India by the assessee in convertible foreign exchange, but does not include freight, telecommunication charges or insurance attributable to the delivery of the articles or things outside India.
4. Total turnover means the turnover as per books but does not include freight, telecommunication charges or insurance attributable to the delivery of the articles or things outside India.

b) Withdrawal of Exemption in Certain Cases - Section 47A

- 1) If tax on capital gains has been exempt U/S 47 in case of transfer of a capital asset by a holding company to its subsidiary or vice-versa, the capital gains so exempt shall be chargeable to tax in the year of transfer if:
 - i) The holding company does not continue to hold the whole of the share capital of the subsidiary for a period of 8 years from the date of transfer or
 - ii) The transferee company converts the capital asset into stock-in-trade within a period of 8 years from the date of transfer.
- 2) If the condition stipulated regarding the succession of proprietary concern or firm by the company whereby capital gain tax is not levied are not complied with, the benefits availed by the sole proprietor or the firm, as the case may be, shall be deemed to be profit and gains of the successor company chargeable to tax in the year in which the condition in section 47 is violated.

3. (i) The term “Other right of occupancy” mentioned in explanation 1 to section 32(1) will mean any right similar to a lease and will certainly include tenancy rights also. It will also include rights of occupancy arising in the case of ownership flats in cooperative societies / companies / AOPs or rights arising under similar agreements or arrangements. The basic requirement will be that the right must be a right of occupancy and not any other type of right and it must be an enforceable one.

(ii) According to section 49 if the asset is acquired by an assessee by way of gift or will then the cost of acquisition will be the cost to the previous owner. Indexed cost of acquisition means an amount which bears to the cost of acquisition the same proportion as the cost inflation index for the year in which the asset is transferred bears to the cost inflation index for the **first year in which the asset was held by the assessee**” or 1st April 19881 whichever is later. Hence the assessee in the given case can index only from the year 2002-03 and not from 1993-94.

4. The Reverse Mortgage scheme is for the benefit of senior citizens, who own a residential house property. In order to supplement their existing income, they can mortgage their house property with a scheduled bank or housing finance company, in return for a lump-sum amount or for a regular monthly/quarterly/annual income. The senior citizens can continue to live in the house and receive regular income, without the, botheration of having to pay back the loan. The loan will be given up to, say, 60% of the value of residential house property mortgaged.

Also, the bank/housing finance company would undertake a revaluation of the property once every 5 years. The borrower can use the loan amount for renovation and extension of residential property, family’s medical and emergency expenditure etc., amongst others. However, he cannot use the amount for speculative or trading purposes.

The bank will recover the loan along with the accumulated interest by selling the house after the death of the borrower. The excess amount will be given to the legal heirs. However,

before resorting to sale of the house, preference will be given to the legal heirs to repay the loan and interest and get the mortgaged property released.

The Finance Act 2008 has inserted clause (xvi) in section 47 to clarify that any transfer of a capital asset in a transaction of reverse mortgage under a scheme made and notified by the Central Government would not amount to a transfer for the purpose of capital gains.

Further, clause (43) has been inserted in section 10 to provide that the amount received by the senior citizen as a loan, either in lump sum or in installments, in a transaction of reverse mortgage would be exempt from income-tax.

5. Y Ltd - During the previous year 2008-09, the company has distributed assets (being debentures of Z Ltd.) to its shareholders at the time of liquidation. Even if the cost of debentures is Rs. 91lakhs and the market value is Rs. 28lakh, the surplus is not taxable, as by virtue of section 46(1) distribution of capital assets in kind to shareholders at the time of liquidation is not treated as "transfer". It may be noted that the difference of Rs. 19lakh is tax-free income.

Total distribution to shareholders	Rs.
[i.e., debentures in Z Ltd. of Rs. 28lakh +-Rs. 6lakh]	34, 00,000
Out of which treated as dividend under sec 2(22) (c)	
To the extent of accumulated profit	30, 00,000
Tax on dividend [15% + 15% surcharge + 0.495% EC of Rs. 30 lakh]	5, 09,850

Income of X at the time of liquidation of the company

[Assessment year 2009-10]-

Amount received by X on June 30, 2008

(i.e., market value of 1,000 debentures + Rs. 60,000) 3, 40,000

Less: Dividend on which Y Ltd. has dividend tax 3, 00,000

Balance which is treated as full value of consideration on

Transfer of 4,000 shares in Y Ltd. 40,000

Less: Indexed cost of acquisition [Rs. 4,000 X 2 X 582/133]	<u>35,008</u>
Long-term capital gain	4,992
	=====
Income of X/or the assessment year 2010-11-	
Sale consideration of 1,000 debentures of Z Ltd. on April 6, 2009	3, 10,000
Less: Cost of acquisition on June 30, 2008	
(Being the market value on June 30, 2008)	2, 80,000

Short-term capital gain	30,000
	=====

6. (i) Section 115BBC(1) provides for levy of tax @ 30% on anonymous donation received by, inter alia, charitable trusts or institutions referred to in section 11. Further, section 13(7) provides that the exemption provisions contained in sections 11 and 12 shall not be applicable in respect of any anonymous donation liable to tax under section 115BBC. As such, application of the anonymous donations received by the charitable trust for charitable purposes does not confer any exemption from tax. Therefore, the claim for non-taxability under section 115BBC of anonymous donations received by the charitable trust is not valid in law.

(ii) Section 115BBC (2) provides that the provisions contained in section 115BBC (1) relating to the taxability of anonymous donations are not applicable to any trust or institution created or established wholly for religious purposes. As such, the trust established wholly for religious purposes is not liable to be taxed in respect of the anonymous donations received by it. The application or non-application of such anonymous donation for the purposes of trust during the relevant financial year is not germane to the issue of taxability under section 115BBC

7. The Income Tax Act taxes if any income is there in the hands of individuals and it is not bothered about the source of the income or legality of income.

Even though a person is caught with tainted or black money, the Income Tax department will tax him because there is no bearing of illegality over income.

8. The conversion of capital asset into stock in trade is deemed as transfer. Hence Sajjan is liable to pay Capital Gains Tax during the assessment year 2010-11 when he sells the stock in trade. The Fair Market Value on the date of conversion is deemed to be the full value of consideration. The difference between the fair market value and the cost of acquisition is taxed under the head Capital Gains. The difference between the sale value and the fair market value is taxed under the head Profits and Gains from Business or Profession.

PRIME ACADEMY
30th SESSION - PROGRESS TEST
INDIRECT TAX LAWS

No.of.pages: 2

Total Marks: 75
Time Allowed: 2Hrs

PART – A

2.5 x 10 = 25 Marks

- (1) Place of Removal under Central Excise means
- (a) Removing the goods from the place of distributor
 - (b) Removing the goods from the place of customs station
 - (c) Removing the goods from the place of factory
 - (d) None of the above
- (2) The excise duty on alcoholic goods manufactured by the manufacturer is payable to
- (a) State Government
 - (b) Central Government
 - (c) Corporation
 - (d) Local authority
- (3) At the time of manufacture of product X attracts 14% BED. At the time of removal the rate of duty is 8%. Which is the duty attracts for the product X
- (a) 14%
 - (b) 8%
 - (c) 11% (Average)
 - (d) Zero (Because the rate has changed)
- (4) Goods specified under Standards of Weights and Measures Act, 1976 as well as in the notification issued by the Government of India along with rate of abatement can be assessed under
- (a) Maximum Retail Price
 - (b) Transaction Value
 - (c) Retail Price
 - (d) Whole Sale Price

- (5) Which one of the following will come under the Specific Rate of Duty
- (a) Cigarette product
 - (b) Wood product
 - (c) Plastic product
 - (d) Diesel product
- (6) What percentage should be added to the cost of production in the case of captive consumption
- (a) 15%
 - (b) 10%
 - (c) 0%
 - (d) 20%
- (7) As per Rule 10 of the Central Excise Valuation Rules, the concept of interconnected undertakings means
- (a) Associate companies
 - (b) Group companies
 - (c) Holding and Subsidiary companies
 - (d) None of the above
- (8) A manufacturer purchased inputs from supplier 'ABC Co.'. The invoice was for Rs.11,000, comprising of price of goods as Rs.10,000 and Rs.1,000 as excise duty, which is available as Cenvat credit to the manufacturer. Pass journal entry for the purchase of goods.
- (9) Cenvat Credit is not applicable if the following goods are purchased
- (a) Light Diesel Oil
 - (b) Steel products
 - (c) Plastic products
 - (d) Wood products
- (10) A unit availing SSI exemption can avail of CENVAT credit on capital goods but such credit can be utilized only
- (a) if the value of capital goods exceeds Rs.100 lakh
 - (b) after clearance of Rs. 150 lakh
 - (c) if the capital goods are exported

Answer the following

- (1) Parsavnath Furnishers Limited (PFL) is engaged in procuring the duty paid Office Furniture System/Work Stations (OFS/WS) from the suppliers and erecting and installing them at site of customers, from whom it has procured the orders. After receiving the orders from its clients, a team of engineers prepares a lay out on computer aided design system where ready-made furniture systems and work stations manufactured by independent manufactures/suppliers are superimposed. Thereafter, based on the clients'

Specifications, orders are placed upon the manufacturer of the furniture for each works station. After procuring the various elements of furniture system from the manufacturer, they join the same together according to the site drawing and the project code.

The assessee contends that that they are only marketing OFS/WS. However, the Revenue alleges that PFL is liable to pay duty as the said activity amounts to manufacture. Examine, with reference to a decided case law, if any, whether the Revenue's allegation is tenable in law?

- (2) Surat Cloth Mills delivered 1000 meters of cloth to Purvanchal Readymade Garments on 10.01.2009 from its depot located at Ahmedabad @ Rs. 110 per meter. The goods were dispatched to the depot from the factory located in Surat on 05.01.2009. Ex-factory price on 05.01.2009 was Rs. 90 per meter. The sales of identical variety of cloth effected from Ahmedabad depot on the two relevant dates is as follows:-

On 05.01.2009		On 10.01.2009	
Cloth sold (in meters)	Rate per meter (Rs.)	Cloth sold (in meters)	Rate per meter (Rs.)
100	135	200	120
850	125	1,000	110
500	120	550	115
450	115	375	108

Calculate the assessable value of 1,000 meters of cloth sold by Surat Cloth Mills.

- (3) On account of a prolonged strike in the factory of the ABC Ltd., it is decided to cut down the expenditure incurred on labour, packing, inventory advertising etc. One of the bulk buyers of the ABC Ltd.'s products starts advertising the products purchased from ABC Ltd. in order to boost its sales. The Assistant Commissioner of Excise contends that ABC Ltd. has gradually transferred the expenditure on sales promotion/advertisement of its products to the said buyer and thus, such

expenditure should be treated as additional consideration and should be included in the assessable value of the ABC Ltd.'s products.

Examine the situation with the help of any decided case law.

- (4) A company manufacturing consumer durables has factory in Andhra Pradesh. It has a depot in Maharashtra. Its product 'P' is dispatched to its depots in Maharashtra and sold from the depot to its dealers in Maharashtra. The depot administration expenses are Rs.8,36,880 per annum. These do not include CST Act. The present price for sale from Maharashtra Depot is Rs.22,500, inclusive of transport charges from Andhra Pradesh to Maharashtra. Actual transportation charges from Andhra Pradesh to Maharashtra are Rs.1,000 per piece.

The depot price is inclusive of applicable excise duty @ 16% plus cess as applicable, but exclusive of Maharashtra sales tax. Sale from Maharashtra depot of product P are 2,000 pieces per annum. As an economy measure, it is proposed to close the depot in Maharashtra and make direct sale from Andhra Pradesh to dealers in Maharashtra.

Marketing department has stated that if goods are sold from Andhra Pradesh, total amount Payable by dealers in Maharashtra should remain unaltered. Otherwise, sales will be badly affected.

Taxation department argues that this will reduce the profitability of the product, as the CST payable will have to be borne by the company.

Finance department is of the view that this extra tax burden will get offset by reducing in depot expenses and slight reduction in excise duty quantum.

Evaluate the financial implications to decide whether it will be economical to close the depot in Maharashtra and advise Management about desirability or otherwise of closing the depot. Ignore effect of Maharashtra Vat, if any

- (5) Power Rise Industrial Corporation (PRIC) provides services from its office located at Saurashtra while its head office is located at Gorakhpur. The excise duty paid at Saurashtra office of PRIC for the month of December '08 is as follows:-

	Rs.
Excise duty paid on:-	
Inputs used in providing output service	
1,80,000	
Capital goods purchased and involved in providing output service	2,50,000
Input services used in output service	4,20,000

The invoices in respect of aforementioned inputs, capital goods and input services are in the name of Gorakhpur office. Compute the amount of the CENVAT credit admissible to Saurashtra office of PRIC for the month of December '08.

PRIME ACADEMY
30th SESSION - PROGRESS TEST
FINAL - INDIRECT TAX LAWS
SUGGESTED ANSWERS

Part – A

(1) **C**

(2) **A**

(3) **B**

(4) **A**

(5) **A**

(6) **B**

(7) **C**

(8)	Purchase Account	Dr. Rs.10,000
	Cenvat Credit Receivable (input goods) Account	Dr. Rs. 1,000
	To sundry creditors Account	Rs.11,000

(Being input goods purchased from ABC Co.)

(9) **A**

(10) **B**

Part – B

1. The Office Furniture System or Work Stations (OFS/WS) was procured by the PFL after payment of duty thereon. Hence, the manufacture has already taken place at the premises of the supplier (i.e. manufacturer). Therefore, nothing new product had come into existence in the hands of assessee (i.e. PFL) at the time of installing the same at the site of customers. Thereby no duty is required to pay by the assessee. From the above it is evident that the revenue allegation is not tenable in the eyes of central excise law.
2. **Assessable value = Rs. 125 x 1000 meters = Rs. 1,25,000.**
3. The contention of the Assistant Commissioner of Central Excise is not correct. Because the manufacture is not insist the buyer to incurred such sales promotion expenses. Therefore the value advertising the products undertaken by the buyers should not be includable in the assessable value of the product manufactured by the ABC Ltd. [*Glass Industries Ltd. v CCE*. 2006 (201) ELT 161 (SC)]
4. Presently, goods are sold from depot. If the sale if from depot, excise duty is payable on the depot price of Rs. 22,500. No deduction of transport cost from Andhra Pradesh to Maharashtra is allowable. Since the price is inclusive of excise duty @ 16.48% (16% plus 2% education cess plus 1% SAH education cess), the duty payable is Rs.3,183.38 and Assessable Value is Rs.19,316.62 After deducting freight expenses of Rs.1,000, present net realization is Rs.18,316.62 per piece.

If goods are sold directly from Andhra Pradesh, CST @ 4% will be payable. The price chargeable to dealers is required t remain unchanged to Rs. 22,500 per piece. If we assume that net sale price from Andhra Pradesh is 'x', then total invoice value to dealers in Maharashtra will be as follows-

Net price of Product A	X
Add- Excise Duty @ 16.48%	0.1648x
Add- CST @ 4% on 1.1648x	0.046492X
Total price	1.211392x

Add- Transport charges	Rs. 1,000
Total Invoice Value	1.211392x + 1,000

Note.—Excise duty and CST are not payable on transport charges, if charged separately in invoice, if sale is from factory.

Now, $1.211392x + 1000 = 22,500$

Hence, $x = \text{Rs. } 17,748.18$

Thus, the realization per piece has reduced from Rs. 18,316.62 to Rs. 17,748.18 per piece. This results in loss of Rs.568.44 per piece. Since sale is 2,000 pieces per annum, total loss per year will be Rs. 11, 36,880. If depot is closed, there will be saving of Rs. 8, 36,880 per annum. Thus, there will be net loss of Rs. 3, 00,000 if the depot is closed and sales are effected directly from Andhra Pradesh. Hence, it is not economical to close the depot.

5. Admissible Cenvat credit to Saurashtra office	Rs.
Inputs used in providing output service	1, 80,000
Capital goods purchased and involved in	
Providing output service 2, 50,000 x 50%	1, 25,000
Input services used in output service	4, 20,000

Total Cenvat credit allowed	7, 25,000
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