

REVISION TEST PAPERS

FINAL COURSE

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PAPER – 5 : COST MANAGEMENT

QUESTIONS

1. (a) What do you understand by MRP? What are its objectives?
- (b) "In case of a multi product company, Pareto Analysis is of immense help for pricing purposes". Discuss.
- (c) Describe the concept of Back flushing as used in the JIT system. What problems need to be addressed before implementing such a concept? Briefly discuss.
2. (a) Somesh plans to open a Rest house which shall be able to accommodate 6 to 15 guests at a charge of Rs 100 per week. Somesh estimates to earn a contribution margin of Rs 57 per guest and shall have to pay fixed expenses relating to rent equaling Rs 4,000 per annum. In addition Rs 1,000 per annum shall be paid to an outside contractor for general maintenance. Somesh estimates that as long as 10 guests are accommodated, the fixed cost of supervision would be Rs. 11,000 for 30 weeks. However, in case guests exceed 10 numbers, addition fixed cost of Rs. 200 per week will have to be incurred for the entire 30 week period

You are required to tabulate the figures to find out the Break-even Point.

- (b) Two manufacturing companies which have the following operating details decide to merge:

	Company 1	Company 2
Capacity utilization %	90	60
Sales (Rs. lakhs)	540	300
Variable Costs (Rs. lakhs)	396	225
Fixed Costs (Rs. lakhs)	80	50

Assuming that the proposal is implemented, calculate:

- (i) Break even sales of the merged plant and the capacity utilization at that stage.
- (ii) Profitability of the merged plant at 80% capacity utilization.
- (iii) Sales turnover of the merged plant to earn a profit of Rs.75 lakhs.
- (iv) When the merged plant is working at a capacity to earn a profit of Rs. 75 lakhs, what percentage increase in selling price is required to sustain an increase of 5% in fixed overheads.
3. (a) The investment for a project is Rs. 20 cr. The selling price per unit shall be Rs 400 with a variable cost of Rs.240 and fixed cost of Rs. 23, 00,000 per annum. If the required rate of return is 12%, what will be the BEP for a life span of 6 yrs?.
- (b) If the project building period is 2 years with 60% of capital invested in the 1st year, what is the project BEP production & sale volume?
4. What do you understand by a Balanced Scorecard? Give reasons why Balanced Scorecards sometimes fail to provide for the desired results. Do you think that such a scorecard is useful for external reporting purposes?
5. ABC Ltd manufactures Product S for national distribution in India. The standard and actual costs for the manufacture of Product S are as follows:

	Standard Costs	Actual Costs
Direct materials	1,500 kgs at Rs. 35	1,600 kgs at Rs. 32
Direct labour	4,800 hours at Rs. 11	4,500 hours at Rs. 11.80
Factory overhead	Rates per labour hour, based on 100% of normal capacity of 5,500 labour hours:	

Variable cost, Rs. 2.40

Rs. 12,300 variable cost

Fixed cost, Rs. 3.50

Rs. 19,250 fixed cost

Instructions:

1. Determine the quantity variance, price variance, and total direct materials cost variance for Product S.
2. Determine the time variance, rate variance, and total direct labour cost variance for Product S.
3. Determine the controllable variance, volume variance, and total factory overhead cost variance for Product S.
6. What do you understand by CVP analysis. Discuss briefly the assumptions underlying the concept.
7. The Production Manager at Gemini Machines Limited has been asked to present information about the times and costs for the development of a new machine that the company may choose to manufacture. The Managing Director requires accurate time and cost estimates since the project will involve a fixed-fee contract offering no provisions for later re-negotiation, even in the event of modifications.

	Activity	Preceding activities	Duration (weeks)	Cost (Rs. '000)
A	Obtain engineering quotes	I	1	4
B	Sub-contract specifications	A, J	4	8
C	Purchase of raw materials	—	3	24
D	Construct prototype	I	5	15
E	Final drawings	I	2	6
F	Fabrication	H	6	30
G	Special machine study	—	4	12
H	Sub-contract work	B, E	8	40
I	Preliminary design	G	2	8
J	Vendor evaluation	C, D	3	3

The Production Manager has been asked to identify the critical activities, to determine the shortest project duration and to provide a week-by-week cost schedule.

Required:

- (a) Draw a network to represent the inter-relationships between the activities indicated, and insert earliest and latest event times throughout.
- (b) Determine the critical path and the shortest possible duration of the project.
- (c) Assuming each activity commences at the earliest start date, and that for each activity the cost is incurred evenly over its duration, construct a week-by-week schedule of cash flows.

The project is to be financed by Rs. 50,000 available initially, a further Rs. 50,000 available at the start of week 9 and the final Rs. 50,000 available from week 20.

Identify any particular problems and suggest solutions.

8. You are the manager of a paper mill (XYZ Ltd) and have recently come across a particular type of paper, which is being sold at a substantially lower rate by another company, ABC Ltd, than the price charged by your own mill. The value chain for one use of one tonne of such paper for ABC Ltd is as follows,

ABC Ltd. —————> Merchant —————> Printer —————> Customer

ABC Ltd sells this particular paper to the merchant at the rate of Rs. 1,466 per tonne . ABC Ltd pays for the freight which amounts to Rs. 30 per tonne. Average returns and allowances amount to 4% of sales and approximately equals Rs. 60 per tonne.

The value chain of your company, through which the paper reaches the ultimate customer is similar to the one of ABC Ltd. However, your mill does not sell directly to the merchant, the latter receiving the paper from a huge distribution center maintained by your company at Haryana. Shipment costs from the mill to the Distribution Center amount to Rs. 11 per tonne while the operating costs in the Distribution Center have been estimated to be Rs. 25 per tonne. The return on investments required by the Distribution Center for the investments made amount to an estimated Rs. 58 per tonne.

You are required to compute the "Mill manufacturing Target Cost" for this particular paper for your company. You may assume that the return on the investment expected by your company equals Rs. 120 per tonne of such paper.

9. Noida Camera Company has received a special order for photographic equipment it does not normally produce. The company has excess capacity, and the order could be manufactured without reducing production of the firm's regular products. Discuss the relevance of each of the following items in computing the cost of the special order
 1. Equipment to be used in producing the order has a book value of Rs. 2,000. The equipment has no other use for Noida Camera Company. If the order is not accepted, the equipment will be sold for Rs. 1,500. If the equipment is used in producing the order, it can be sold in three months for Rs. 800.
 2. If the special order is accepted, the operation will require some of the storage space in the company's plant. If the space is used for this purpose, the company will rent storage space temporarily in a nearby warehouse at a cost of Rs. 18,000. The building depreciation allocated to the storage space to be used in producing the special order is Rs. 12,000.
 3. If the special order is accepted, it will require a subassembly. Noida Camera can purchase the subassembly for Rs. 24.00 per unit from an outside supplier or make it for Rs. 30.00 per unit. The Rs. 30.00 cost per unit was determined as follows:

	Rs.
Direct material	10.00
Direct labour	6.00
Variable overhead	6.00
Allocated fixed overhead	<u>8.00</u>
Total unit cost of subassembly	<u>30.00</u>

10. (a) Discuss briefly the various methods of Transfer Pricing known to you.
- (b) Stellar Systems Company's Microprocessor Division sells a computer module to the company's Guidance Assembly Division, which assembles completed guidance systems. The Microprocessor Division has no excess capacity. The computer module costs Rs. 10,000 to manufacture, and it can be sold in the external market to companies in the computer industry for Rs. 13,500.
 You are required to compute the transfer price for the computer module using the general transfer-pricing rule.
11. (a) "Costs may be classified in a variety of ways according to their nature and the information needs of the management." Explain.
- (b) Indicate the major areas of short-term decisions in which differential cost analysis is useful.
- (c) "Relevant cost analysis helps in drawing the attention of managers to those elements of cost which are relevant for the decision." Comment.

12. (a) Indicate the possible disadvantages of treating divisions as profit centres.
 (b) Explain the role of bench marking in continuous improvement in an organisation.
13. ABC Ltd manufactures a product '1+7 ASCS' at its plant at Faridabad, the maximum capacity of which is 200 units per month. Details of raw material which go into the making of 1 unit of '1+7 ASCS' are provided to you below;

S. No.	Raw Material description	Standard quantity per finished unit (No)	Standard purchase price per unit (Rs 00)
1	A	1	6
2	B	2	5
3	C	3	4
4	D	4	3
5	E	5	2
6	F	6	1

Standard Fixed overheads are Rs. 20,00,000 per month whereas the standard variable overhead rate has been estimated as equal to Rs. 1,400 per unit of finished good. You are required to compute the

- (a) standard cost of the product
 (b) compute the production volume variance in case the company produces and sells only 100 units of finished goods in the concerned month.
 (c) compute the usage and material price variances considering the following actual data(actual production and sale: 100 units)

Raw material description	Actual quantity consumed (Nos)	Actual price(Rs 00)
A	102	7
B	201	6
C	310	5
D	415	4
E	540	3
F	610	2

- (d) Assuming no deviations in the actual selling price (Rs 30,000) and the actual overheads from what was projected in standards , you are required to compute actual profits .
14. At the beginning of the year, Kare Company initiated a quality-improvement program. Considerable effort was expended to reduce the number of defective units produced. By the end of the year, reports from the production manager revealed that scrap and rework had both decreased. The president of the company was pleased to hear of the success but wanted some assessment of the financial impact of the improvements. To make this assessment, the following financial data were collected for the current and preceding years:

	Preceding year	Current year
	Rs.	Rs.
Sales	10,000,000	10,000,000
Scrap	4,00,000	3,00,000
Rework	6,00,000	4,00,000
Product inspection	1,00,000	1,25,000

Product warranty	8,00,000	6,00,000
Quality training	40,000	80,000
Materials inspection	60,000	40,000

Required:

- Classify the costs as prevention, appraisal, internal failure, or external failure.
 - Compute quality cost as a percentage of sales for each of the two years. By how much has profit increased because of quality improvements? Assuming that quality costs can be reduced to 2.5 per cent of sales, how much additional profit is available through quality improvements (assume that sales revenues will remain the same)?
15. A company has four factories situated in four different locations in the country and four sales agencies located in four other locations in the country. The cost of production (Rs. per unit), the sale price (Rs. per unit), shipping cost (Rs. per unit) in the cells of matrix, monthly capacities and monthly requirements are given below:

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

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

16. IBM Ltd. Manufactures and sells computers peripherals to several retail outlets throughout the country. Amar is the manager of the printer division. Its two largest-selling printers are P1 & P2. The manufacturing cost of each printer is calculated using IBM's activity based costing system. IBM has one direct manufacturing cost category (direct materials) and the following five indirect manufacturing cost pools.

Indirect manufacturing cost pool	Allocation Base	Allocation Rate (Rs.)
1. Materials handling	No. of parts	Rs. 1.20 per part
2. Assembly management	Hours of assembly time	Rs. 40 per hour of assembly time
3. Machine insertion of parts	No. of machine inserted parts	Rs. 0.70 per machine inserted part
4. Manual insertion of parts	No. of manually inserted parts	Rs. 2.10 per manually inserted part
5. Quality testing	Hours of quality testing time	Rs. 25 per testing hour.

Product characteristics of P1 and P2 are as follows:

Product	P1	P2
Direct materials costs	Rs. 407.50	Rs. 292.10
Number of parts	85	46

Hours of assembly time	3.2	1.9
Number of machine – inserted parts	48	31
Number of manually inserted parts	36	15
Hours of quality testing time	1.4	1.1

A foreign competitor has introduced products very similar to P1 and P2. Given their announced selling prices and to maintain his company's market share and profits, Amar estimates the P1 to have manufacturing cost of approximately Rs. 680 and P2 to have a manufacturing cost of approximately Rs. 390. He calls a meeting of product designers and manufacturing personnel at the printer division. They all agree to have the Rs. 680 and Rs. 390 figures become target costs for designed version of P1 and P2 respectively. Product designers examine alternative ways of designing printer with comparable performance but lower costs. They come up with the following revised designs for P1 and P2 (termed P1 – REV and P2 – REV, respectively)

Particulars	P1 – REV	P2 – REV
Direct materials cost	Rs. 381.20	Rs. 263.10
Number of parts	71	39
Hours of assembly time	2.1	1.6
Number of machine – inserted parts	59	29
Number of manually – inserted parts	12	10
Hours of quality testing time	1.2	0.9

Required:

- Compute the present costs of products P1 and P2 using ABC system.
- Compute the manufacturing costs of P1 – REV and P2 – REV. How do they compare with the Rs. 680 and Rs. 390 target costs?

17. A manufacturer of the firm is investigating the inventory situation of his company. Distribution of daily demand is

Demand (units)	No. of Days
5	15
6	25
7	30
8	18
9	8
10	4

The lead time distribution in days is given below

Lead time	Probability
3	.2
4	.3
5	.35
6	.15

The ordering cost is Rs. 100 per order; the holding cost is Rs. 3 per unit per day and the shortage cost is Rs. 20 per unit, representing the loss in profits.

Using simulation determine the total inventory cost for specific reorder level and reorder quantity.

Assume the opening inventory is 25 units, the reorder level is 20 units and the reorder quantity is 40 units.

18. The occurrence of the rain in a day is dependent upon whether it rained on the previous day. If it rained on the previous day the rain distribution is given by

Event	Probability
No rain	.50
1 cm rain	.25
2 cm rain	.15
3 cm rain	.05
4 cm rain	.03
5 cm rain	.02

If it did not rain on the previous day the rain distribution is given by

Event	Probability
No rain	.75
1 cm rain	.15
2 cm rain	.06
3 cm rain	.04

Simulate the city's weather for 10 days and determine by simulation the total days without rain as well as the total rain fall during the period. Use the following random numbers

76 78 84 75 02 86 02 78 07 63

For simulation, assume that for the first day of the simulation it had not rained before.

19. An organisation producing 4 different products viz. A, B, C and D having 4 operators viz. P, Q, R and S, who are capable of producing any of the four products, works effectively for 7 hours a day. The time (in minutes) required for each operator for producing each of the product are given in the cells of the following matrix along with profit (Rs. per unit):

Operator	Product			
	A	B	C	D
P	6	10	14	12
Q	7	5	3	4
R	6	7	10	10
S	20	10	15	15
Profit (Rs./Unit)	3	2	4	1

Find out the assignment of operators to products which will maximize the profit.

20. (a) What do you understand by project crashing using network analysis. Discuss briefly giving graph for cost slope.
(b) Discuss briefly the limitations of linear programming.

SUGGESTED ANSWERS/HINTS

1. (a) Material Requirements Planning (MRP) is a software based production planning and inventory control system used to manage manufacturing processes. Although it is not common nowadays, it is possible to conduct MRP by hand as well.

MRP is designed to answer three questions: what is needed, how much is needed, and when is it needed. The primary inputs of MRP are a bill of materials, which tells what goes into a finished product; a master schedule, which tells how much finished product is desired and when; and an inventory-records file, which tells how much inventory is on hand or on order. This information is processed, using various computer programs to determine the net requirements for each period of the planning horizon. Outputs from the process include planned-order schedules, order releases, changes, performance-control reports, planning reports, and exception reports.

An MRP system is intended to simultaneously meet the following 3 objectives:

1. Ensure materials and products are available for production and delivery to customers.
2. Maintain the lowest possible level of inventory.
3. Plan manufacturing activities, delivery schedules and purchasing activities.

For further details please refer to chapter 10 of the Institute's Cost Management book.

- (b) In the case of firm dealing with multi products, it would not be possible for it to analyse price-volume relationship for all of them. Pareto Analysis is used for analysing the firm's estimated sales revenue from various products and it might indicate that approximately 80% of its total sales revenue is earned from about 20% of its products. Such analysis helps the top management to delegate the pricing decision for approximately 80% of its product to the lower level of management, thus freeing them to concentrate on the pricing decisions for products approximately 20% of which is essential for the company's survival. Thus, a firm can adopt more sophisticated pricing methods for small proportion of products that jointly account for 80% of total sales revenue. For the remaining 80% products, which account for 20% of the total sales value the firm may use cost, based pricing method.
- (c) Traditional accounting systems record the flow of inventory through elaborate accounting procedures. Such systems are required in those manufacturing environment where inventory/WIP values are large. However, since JIT systems operate in modern manufacturing environment characterized by low inventory and WIP values, usually also associated with low cost variances, the requirements of such elaborate accounting procedures does not exist.

Back flushing requires no data entry of any kind until a finished product is completed. At that time the total amount finished is entered into the computer system which is multiplied by all components as per the Bill of materials (BOM) for each item produced. This yields a lengthy list of components that should have been used in the production process and this is subtracted from the opening stock to arrive at the closing stock to arrive at the closing stock/inventory.

The problems with back flushing that must be corrected before it works properly are:

- (i) The total production quantity entered into the system must be absolutely correct, if not, then wrong components and quantities will be subtracted from the stock.
- (ii) All abnormal scrap must be diligently tracked and recorded. Otherwise materials will fall outside the back flushing system and will not be charged to inventory.
- (iii) Lot tracing is impossible under the back flushing system. This is required when a manufacturer needs to keep records of which production lots were used to create a product in case all the items in a lot need be recalled.
- (iv) The inventory balance may be too high at all times because the back flushing transactions that relieves inventory usually does so only once a day, during which time other inventory is sent to the production process. This makes it difficult to maintain an accurate set of inventory records in the warehouse.

2. (a)

Rest house
Statement Showing Costs and Income

¹ No. of Guests	Income per annum	Variable Costs Rs.	Contribution Rs.	Fixed cost (Note ³ and ⁴)	Surplus / (Deficit) Rs.
6	18,000	7,740	10,260	³ 16,000	(5,740)
7	21,000	9,030	11,970	16,000	(4,030)
8	24,000	10,320	13,680	16,000	(2,320)
9	27,000	11,610	15,390	16,000	(610)
10	30,000	12,900	17,100	16,000	1,100
11	33,000	14,190	18,810	⁴ 22,000	(3,190)
12	36,000	15,480	20,520	22,000	(1,480)
13	39,000	16,770	22,230	22,000	230
14	42,000	18,060	23,940	22,000	1,940
15	45,000	19,350	25,650	22,000	3,650

Working Notes

¹ 6 persons x Rs. 100 x 30 weeks = Rs. 18,000 and so on² No of persons x Rs. 43 x 30 weeks = 7.740 and so on³ Rs. 11,000 + Rs. 4,000 + Rs. 1,000 = Rs. 16,000⁴ When guests are more than 10, Fixed Cost Rs. 16,000 (as above) + Rs. 200 x 30 = Rs. 22,000

(b)

	Company 1	Company 2	Total (merged plant)
1. Capacity utilization	100%	100%	100%
2. Sales	600	500	1,100
3. Variable costs	440	375	815
4. Contribution	160	125	285
5. Fixed Cost	80	50	130
6. Profit	80	75	155
7. P/V Ratio (Merged Plant)	$(285 \div 1100) \times 100 = 25.91\%$		
8. BEP of the Merged plant	$130 \div .2591 = \text{Rs. } 501.74$		
9. Capacity utilization at BEP	$501.74 \div 1,100 = 45.61\%$		
(ii) Profitability of the merged plant of 80% capacity			

	Rs. in lakhs
Sales (1,100 x 80%)	880
Variable cost	652
Contribution	228
Fixed Cost	130
Profit	98
Profit as a % Sales	11.14%

(iii) Sales required for earning a profit of Rs. 75 lakhs

Contribution request = Fixed cost + Desired profit = 130 lakhs + 75 lakhs = Rs 205 lakhs

P/V Ratio = 25.91%

Desired sales Level = Desired contribution ÷ P/V Ratio

Desired sales Level = Rs. 205 lakhs ÷ 25.91% = Rs. 791.20 lakh

(iv) Percentage increase in Selling Price to sustain 5% increase in F.O. (with Rs. 75 lakhs profit)

Fixed overhead = Rs. 130 lakhs

5 % increase = Rs. 6.5 lakhs (Rs 130 lakhs x 0.05)

Sales = Rs. 791.20 lakhs (Given)

Hence % increase in S.P.= $(6.5 \div 791.20) \times 100 = 0.8215\%$

3. (a) Investment = Rs. 20 Crores

Rs.

Selling price/unit 400

Variable cost/unit 240

Contribution/unit 160

Fixed cost = 23 lakhs; Life – 6 years; Rate of return = 12%

BEP = $\{(20 \text{ cr.} \div 4.114) + 23 \text{ lakhs}\} \div 160 = 3,18,408 \text{ units}$

(b) All cash flows occur at the end of the year (assumption of DCF technique)

$\therefore$ Interest at $y_0 = 20 \text{ Cr.} + 12 \text{ Cr.} \times 12\%$

= Rs. 21.44 Cr.

$\therefore$ BEP = $\{(21.44 \text{ cr.} \div 4.1114) + 23 \text{ lakhs}\} \div 160$

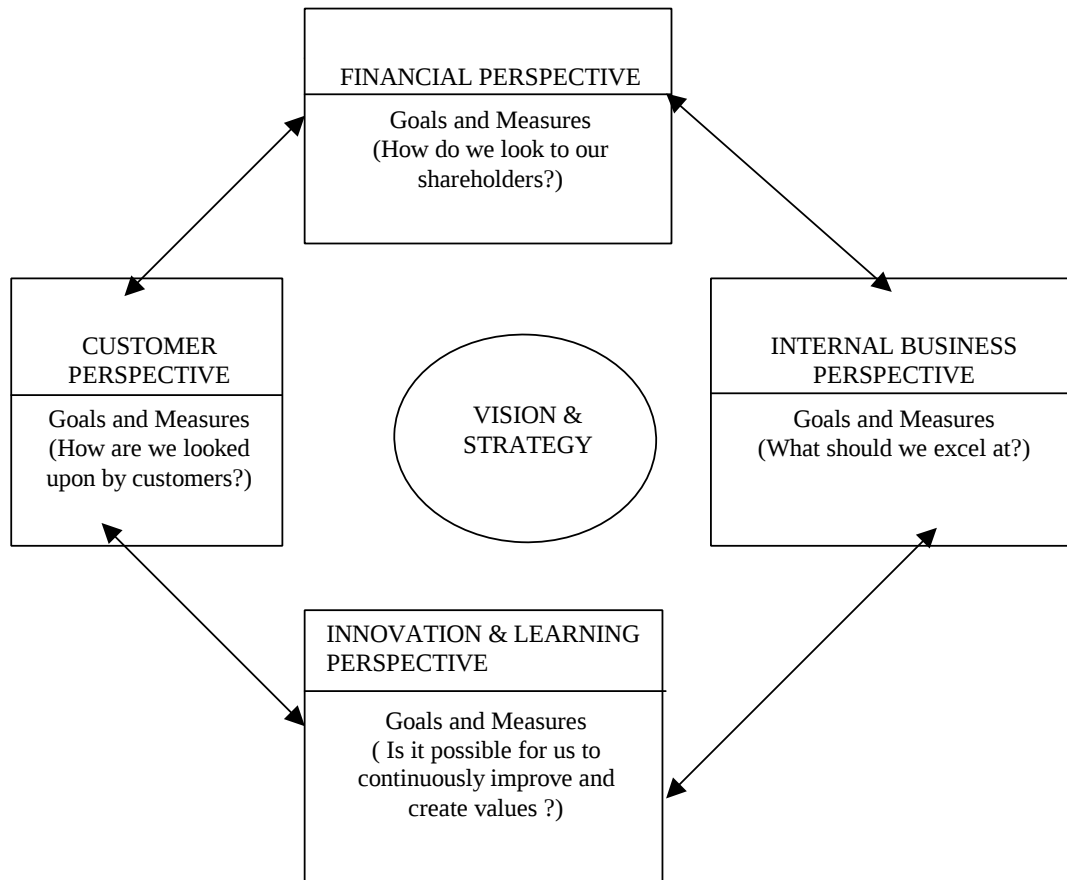
= 3,40,299 units

4. The Balanced Scorecard can be defined as 'an approach to the provision of information to management to assist strategic policy formulation and achievement. It emphasises the need to provide the user with a set of information, which addresses all relevant areas of performance in an objective and unbiased fashion. The information provided may include both financial and non financial elements, and cover areas such as profitability, customer satisfaction, internal efficiency and innovation'.

It is clear from the above definition that the central idea of the Balanced Scorecard is that managers should develop the measures on which they manage the business from four different perspectives:

1. customer satisfaction
2. internal business process e.g., operating cycle time.
3. kaizen approach (can we continue to improve and create value)
4. financial e.g., operating income by segments.

The following figure summarises the ideas of a Balanced Scorecard:



According to Kaplan and Norton, the ultimate result of using the Balanced Scorecard approach should be an improved long-term financial performance. Since the scorecard gives equal importance to the relevant non – financial measures, it should discourage the short termism that leads to cuts in spending on new product development, human resource development etc which are ultimately detrimental for the future prospects of the company.

The responsibility to devise and implement a Balanced Scorecard should be that of the managers working with the business. Since every company is different, it shall need to work out for itself the various financial and non – financial measures, which need to be focussed upon for its own development. Since the Balanced Scorecard is recommended as a management tool used both for internal and external reporting purposes, it is again the manager's responsibility to decide as to what information needs to be disclosed and how any problems of confidentiality can best be overcome.

The following are some reasons why Balanced Scorecards sometimes fail to provide for the desired results;

- The use of non financial measures leads managers to think that they have a Balanced Scorecard already working for strategic purposes.
- Senior executives misguidedly delegate the responsibility of the Scorecard implementation to middle level managers.
- Company's try to copy measures and strategies used by the best companies rather than developing their own measures suited for the environment under which they function.
- There are times when Balanced Scorecards are thought to be meant for reporting purposes only. This notion does not allow a Business to use the Scorecard to manage Business in a new and more effective way.

It may be noted that the above-mentioned difficulties refer to the internal use of the Scorecard. It remains a matter of debate whether a Balanced Scorecard is applicable to external reporting. Critics argue that if the Scorecard is indeed a relevant driver of long term performance, shouldn't the information generated be of interest to the investment community? However, it has been noticed that the Scorecard does not translate easily to the investment community for the simple reason that it makes sense for individual business units and different individual projects rather than the company as a whole. Most companies have different divisions with their own mission and strategy and hence these individual scorecards cannot be aggregated into an overall corporate scorecard. However, in case the company somehow manages to overcome such a problem and indeed use its Scorecard for external reporting, it may end up passing sensitive information to its competitors which may end up being detrimental to the company in the long run. However, with changes in the thinking process of the investment community, such strategic reporting could well be accepted in the near future.

For a further understanding of the concept, please refer to chapter 14 of the Institute's Cost Management book.

5. 1. Direct Materials Cost Variance

Quantity Variance:

Actual quantity	1,600 kgs
Standard quantity	1500 kgs
Variance – unfavourable	100 kgs × Std price, Rs 35 =(Rs. 3,500)

Price Variance:

Actual price	Rs. 32.00 per kg
Standard price	Rs 35
Variance – favourable	Rs 3 per kg × Actual Qty, 1600 = 4,800
Total direct materials cost variance – favourable =	Rs. 1,300

2. Direct Labour Cost Variance

Time Variance:

Actual time	4,500 hours
Standard time	4,800 hours
Variance – favourable	300 hours × Std rate, Rs 11 Rs. 3,300

Rate Variance:

Actual rate	Rs. 11.80
Standard rate	11.00
Variance – unfavourable	Rs 0.80 per hr × Actual time, 4500 hours <u>(3,600)</u>
Total direct labour cost variance - unfavourable	(Rs 300)

3. Factory Overhead Cost Variance

Variable factory overhead – controllable variance:

Actual variable factory overhead cost incurred	Rs. 12,300
Budgeted variable factory overhead for 4,800 hours	<u>11,520*</u>
Variance – unfavourable	(Rs. 780)

Fixed factory overhead – volume variance:

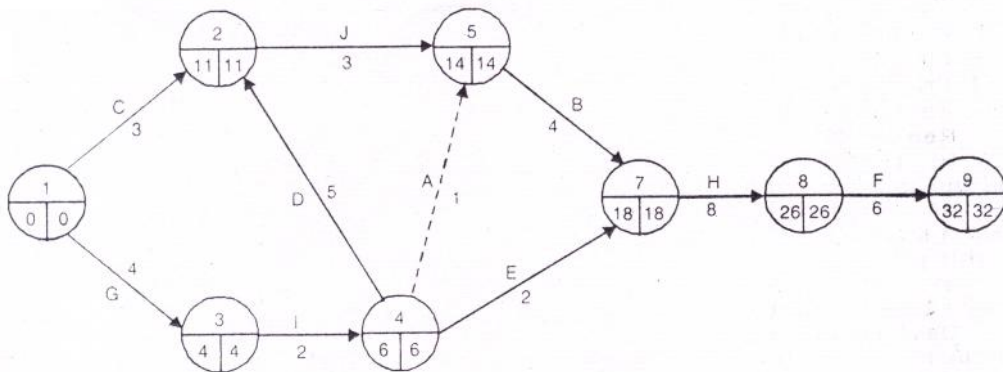
Budgeted hours at 100% of normal capacity	5,500 hours
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Standard hours for actual production	<u>4,800</u>
Productive capacity not used	700 hours
Standard fixed factory overhead cost rate	<u>× Rs. 3.50</u> hours
Variance – unfavourable	<u>(2,450)</u>
Total factory overhead cost variance – unfavourable	<u>Rs. 3,230</u>
*4,800 hours × Rs. 2.40 = Rs. 11,520	

6. As the name suggests, cost volume profit (CVP) analysis is the analysis of three variables cost, volume and profit. Such an analysis explores the relationship between costs, revenue, activity levels and the resulting profit. It aims at measuring variations in cost and volume.

CVP analysis is based on the following assumptions:

1. Changes in the levels of revenues and costs arise only because of changes in the number of product (or service) units produced and sold – for example, the number of television sets produced and sold by Sony Corporation or the number of packages delivered by Overnight Express. The number of output units is the only revenue driver and the only cost driver. Just as a cost driver is any factor that affects costs, a revenue driver is a variable, such as volume, that causally affects revenues.
 2. Total costs can be separated into two components; a fixed component that does not vary with output level and a variable component that changes with respect to output level. Furthermore, variable costs include both direct variable costs and indirect variable costs of a product. Similarly, fixed costs include both direct fixed costs and indirect fixed costs of a product.
 3. When represented graphically, the behaviours of total revenues and total costs are linear (meaning they can be represented as a straight line) in relation to output level within a relevant range (and time period).
 4. Selling price, variable cost per unit, and total fixed costs (within a relevant range and time period) are known and constant.
 5. The analysis either covers a single product or assumes that the proportion of different products when multiple products are sold will remain constant as the level of total units sold changes.
 6. All revenues and costs can be added, subtracted, and compared without taking into account the time value of money.
7. (a)



(b) Critical path = G → I → D → J → B → H → F

$$= 4 + 2 + 5 + 3 + 4 + 8 + 6 = 32 \text{ weeks}$$

(c) The start and finish time for each activity (assuming each starts at the EST) are:

Activity	Start	Finish	Cost/week Rs. ('000)
A	6	7	4
B	14	18	2
C	0	3	8
D	6	11	3
E	6	8	3
F	26	32	5
G	0	4	3
H	18	26	5
I	4	6	4
J	11	14	1

A week-by-week schedule is provided by:

Time	Activity	Cost/week Rs. ('000)
0–3	C, G	11
3–4	G	3
4–6	I	4
6–7	D, A, E	10
7–8	D, E	6
8–11	D	3
11–14	J	1
14–18	B	2
18–26	H	5
26–32	F	5

The cash outflows (in Rs. '000), week by week are shown in the following table:

Week	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16
Cost	11	11	11	3	4	4	10	6	3	3	3	1	1	1	2	2
Week	17	18	19	20	21	22	23	24	25	26	27	28	29	30	31	32
Cost	2	2	5	5	5	5	5	5	5	5	5	5	5	5	5	5

The cash outflow in the first eight weeks amounts to Rs. 60,000, which is more than Rs. 50,000 available for these weeks, i.e., budget would have been exceeded in 7th week. However, it is possible to defer activities A and E until week 9 without prolonging the overall project duration. The final Rs. 50,000 available in week 20 in time for all subsequent cash outflows.

8. Computation of Target Cost

	Per tonne (in Rs)
ABC Ltd selling price to the merchant	1,466
Less freight paid by ABC Ltd	(30)
Less normal sales returns and allowances	(60)

XYZ Ltds Capital charge	(120)
Target cost for XYZ Ltd	1,256
Ship to Distribution Centre	(11)
Distribution Centre operating cost	(25)
Subtotal	1,220
Distribution centre capital charge	(58)
Mill target manufacturing cost	1,162

9. (1) The book value of the equipment is a sunk cost, irrelevant to the decision. The relevant cost of the equipment is Rs. 700, determined as follows:

	Rs.
Sales value of equipment now	1,500
Sales value after producing special order	<u>800</u>
Differential cost	<u>700</u>

- (2) The Rs. 12,000 portion of building depreciation allocated to the storage space to be used for the special order is irrelevant. First, it is a sunk cost. Second, any costs relating to the company's factory building will continue whether the special order is accepted or not. The relevant cost is the Rs. 18,000 rent that will be incurred only if the special order is accepted.
- (3) Noida Camera should make the subassembly. The subassembly's relevant cost is Rs. 22.00 per unit.

Relevant Cost of Making Subassembly (per unit)	Rs.	Relevant Cost of Purchasing Subassembly (per unit)	Rs.
Direct material	10.00	Purchase price	<u>24.00</u>
Direct labour	6.00		
Variable overhead	<u>6.00</u>		
Total	<u>22.00</u>		

The unitized fixed overhead, Rs. 8.00, is not a relevant cost of the subassembly. Noida Camera Company's total fixed cost will not change, whether the special order is accepted or not.

10. (a) The methods of pricing usually employed in industry when goods or services are transferred from one unit to the other can be broadly classified under the following three categories:
- Pricing at cost or variants of cost e.g. manufacturing cost; standard cost; full cost and full cost plus mark up.
 - Pricing at market price.
 - Pricing at bargained or negotiated price.
- (b) Transfer price = Outlay cost + Opportunity cost
- $$= \text{Rs. } 10,000 + (\text{Rs. } 13,500 - 10,000)$$
- $$= \text{Rs. } 13,500$$

The Rs. 3,500 opportunity cost of a transfer is the contribution margin that will be forgone if a computer module is transferred instead of sold in the external market

11. (a) Cost classification is the process of grouping costs according to their characteristics. Costs are classified or grouped according to their common characteristics. Costs may be classified according to elements, according to functions or operations, according to their behaviour,

according to controllability or according to normality.

The break up of the aggregate costs into relevant types, is an essential pre-requisite of decision making as well as of controlling costs. Classification of costs on different bases is thus necessary for various purposes. For the purpose of decision-making and control, costs are distinguished on the basis of their relevance to different type of decisions and control functions. The importance of distinguishing costs as direct or indirect lies in the fact that direct costs of a product or an activity can be accurately allocated while indirect costs have to be apportioned on the basis of certain assumptions. This is so because direct costs are controllable at the operational level whereas indirect costs are not amenable to such control.

- (b) Cost information is required both for short-term and long-run managerial problems. Differential costs are of particular use in short-term problems which are non-repetitive, one-time, ad-hoc problems. The following are the most common short-term problems and areas where differential cost analysis may be deployed.

1. Accept - or - reject special order decisions.
2. Make - or - buy decisions.
3. Sell- or - process decisions.
4. Reduce - or - maintain price decisions.
5. Add - or - drop product decisions.
6. Operate - or shut down decisions.

- (c) Relevant costs are pertinent or valid costs for a decision. These bear upon or 'influence decision' and are directly related to the decisions to be made. These are critical to the decision, and have significance for it. These are the costs which generally respond to managerial decision making, and have significance in arriving at correct conclusions. These costs are capable of making a difference in user-decisions and enter into a choice between alternative courses of action. In specific terms, relevant costs for decisions are defined as "expected future costs that will differ under alternatives".

Relevant costs are futuristic in nature. These are the costs that are expected to occur during the time period covered by the decision. These costs are different between alternatives being considered. Only costs that differ among decision alternatives are relevant to a decision.

12. (a) The possible disadvantages of treating divisions as profit centres are as follows:

1. Divisions may compete with each other and may take decisions to increase profits at the expense of other divisions thereby overemphasizing short term results.
2. It may adversely affect co-operation between the divisions and lead to lack of harmony in achieving. Organisational goals of the company. Thus it is hard to achieve the objective of goal congruence.
3. It may lead to reduction in the company's overall total profits.
4. The cost of activities which are common to all divisions may be greater for decentralised structure than for centralised structure. It may thus result in duplication of staff activities.
5. Top management delegates decision making to divisional managers. There are risks of mistakes committed by the divisional managers which the top management, may avoid.
6. Series of control reports prepared for several departments may not be effective from the point of view of top management.
7. It may under utilise corporate competence.
8. It leads to complications associated with transfer pricing problems.
9. It becomes difficult to identify and define precisely suitable profit centres.

10. It confuses division's results with manager's performance.

- (b) Bench marking is a technique which is being adopted as a mechanism for achieving continuous improvement. It is a continuous process of measuring a company's products, services or activities against the other best performing organizations either internal or external to the company. The objective is to ascertain how the processes and activities can be improved. The latest developments, best practices and model examples can be incorporated within various operations of the business of the company. It represents an ideal way of achieving high competitive standards.

13. (a) Standard Cost Sheet

Description	Cost per unit of Finished Good
Standard Raw Material Cost	Rs 5,600
Variable Overheads	Rs 1,400
Standard Fixed Overheads	Rs 10,000
Standard Cost per Unit of Finished Good	Rs 17,000

(b) Production Volume Variance

Unutilised capacity × Standard Fixed Cost per Finished Good

$$100 \times \text{Rs } 10,000 = \text{Rs } 10,00,000 \text{ Adverse}$$

(c) Usage and Material Price Variance (Actual Production : 100 Units)

Raw Mat.	Std Qty/FG	Std Qty on actual prod	Actual Qty on actual prod	Act Price per Ut of RM(Rs)	Std Price per Ut of RM(Rs)	Usage Variance(Rs)	Price Variance(Rs)
A	1	100	102	700	600	(1,200)	(10,200)
B	2	200	201	600	500	(500)	(20,100)
C	3	300	310	500	400	(4,000)	(31,000)
D	4	400	415	400	300	(4,500)	(41,500)
E	5	500	540	300	200	(8,000)	(54,000)
F	6	600	610	200	100	(1,000)	(61,000)
						(19,200)	(2,17,800)

(d)

Standard Profit (Rs 13,000 × 100)	Rs 13,00,000
Usage Variance	(19,200)
Price Variance	(2,17,800)
Production Volume Variance	(10,00,000)
Actual Profit	63,000

14. 1. Prevention costs: Quality training

Appraisal costs: Product inspection and materials inspection

Internal failure costs: Scrap and rework

External failure costs: Warranty

2. Preceding year – Total quality costs: Rs. 20,00,000; percentage of sales: 20 per cent (Rs. 20,00,000/Rs. 10,00,000). Current year – Total quality costs: Rs. 15,45,000; percentage of

sales: 15.45 per cent (Rs. 15,45,000/Rs. 10,000,000). Profit has increased by Rs. 4,55,000. If quality costs drop to 2.5 per cent of sales, another Rs. 12,95,000 of profit improvement is possible (Rs. 15,45,000 – Rs. 2,50,000).

15. The given information can be tabulated in following transportation problem

Profit Matrix

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

Where entries in the cells of the above table indicate profit per unit received by selling one unit of item from factory i ($i=A, B, C, D$) to j^{th} sales agency ($j=1,2,3,4$). The profit per unit is calculated using the following formula:

$$\text{Profit} = \text{Sales Price} - (\text{Cost of Production} + \text{Shipping Cost})$$

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

Loss Matrix

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

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

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

The initial solution is as given below which is tested for optimality. There are $m+n-1=7$ independent allocations.

Let us introduce $u_i, v_j, i = (1,2,3,4); j = (1,2,3,4)$ such that $\Delta_{ij} = c_{ij} - (u_i + v_j)$ for allocated cells. We assume $u_4=0$ and remaining u_i 's, v_j 's and Δ_{ij} 's are calculated as below:

Factory	Sales Agency				u_i 's
	1	2	3	4	
A	1 6	10 2	0 0	1 5	-7
B	-2 7	1 7	-1 3	15 8	-3
C	2 9	3 9	18 4	-0 12	-3
D	6 12	2 9	-2 5	+0 11	0
	12	9	7	11	

Since some of the Δ_{ij} 's are negative, therefore, the above solution is not optimal. Introduce in the cell (D, 3) with the most negative Δ_{ij} , an assignment θ . The value of θ and the reallocated solution as obtained from above is given below. The values of u_i 's, v_j 's are also calculated. The solution satisfies the conditions of optimality. The condition $\Delta_{ij} = c_{ij} - (u_i + v_j) \geq 0$ for non allocated cells is also satisfied.

Factory	Sales Agency				u_i 's
	1	2	3	4	
A	3 6	10 2	2 0	1 5	-7
B	0 7	1 7	1 3	15 8	-3
C	8 9	1 9	12 4	2 12	-1
D	2 12	2 9	6 5	7 11	0
v_j 's	10	9	5	11	

Since all Δ_{ij} 's for non basic cells are positive, therefore the solution obtained above is an optimal one. The allocation of factories to sales agencies and their profit amount is given below:

Factory	Sales Agency	Profit	
A	2	$10 \times \text{Rs } 7$	= Rs. 70
B	4	$15 \times \text{Rs } 1$	= Rs. 15
C	1	$8 \times \text{Rs } 0$	= Rs. 0
C	3	$12 \times \text{Rs } 5$	= Rs. 60
D	2	$2 \times \text{Rs } 0$	= Rs. 0
D	3	$6 \times \text{Rs } 4$	= Rs. 24
D	4	$7 \times \text{Rs}(-2)$	= -Rs. 14
			= Rs. 155

Since one of the Δ_{ij} 's is zero, the optimal solution obtained above is not unique. Alternate solution also exists.

16.

	P1	P2
	Rs/unit	Rs./unit
Material	407.5	292.1
Overhead-Material handling	$85 \times 1.2 = 102$	$46 \times 1.2 = 55.2$
Assembly Management	$40 \times 3.2 = 128$	$40 \times 1.9 = 76$
Machine insertion	$48 \times 0.7 = 33.6$	$31 \times 0.7 = 21.7$
Manual insertion	$36 \times 2.1 = 75.6$	$25 \times 2.1 = 52.5$
Quality testing	$1.4 \times 25 = 35$	$1.1 \times 25 = 27.5$
Present cost	781.70	504.00
Target cost	680.00	390.00
	Revised P1	Revised P2
	Rs./unit	Rs./unit
Direct material	381.20	263.10
Overhead:		
Material handling	$(71 \times 1.2) = 85.2$	$(39 \times 1.2) = 46.8$
Assembly hour	$(2.1 \times 40) = 84.0$	$(1.6 \times 40) = 64.0$
Machine inspection	$(59 \times 0.7) = 41.3$	$(29 \times 0.7) = 20.30$
Manual inspection	$(12 \times 2.10) = 25.2$	$(10 \times 2.10) = 21.00$
Quality testing	$(1.2 \times 25) = 30.00$	$(0.9 \times 25) = 22.50$
Estimated cost	646.90	437.70
Target cost	680.00	390.00
	Achieved	Not achieved

17. The random number intervals are determined in the first place as shown in table 1 and 2

Table 1: Random Number Intervals for Demand (units)

Demand	No. of Days	Prob.	Cum. Prob.	Random No. Interval
5	15	.15	.15	00-14
6	25	.25	.40	15-39
7	30	.30	.70	40-69
8	18	.18	.88	70-87
9	8	.08	.96	88-95
10	4	.04	1.00	96-99

Table 2 : Random Number Intervals for Lead Time (in days)

Lead time	Probability	Cum. Probability	Random Number Interval
3	.2	.20	00-19
4	.3	.50	20-49
5	.35	.85	50-84
6	.15	1.00	85-99

Table 3 : Simulation Worksheet

Trials	Opening Balance	Random No.	Demand	Closing Balance	Random No.	Lead Time	Ordering Cost	Holding Cost	Shortage Cost
1	25	69	7	18	81	5	100	54	
2	18	61	7	11				33	
3	11	83	8	3				9	
4	3	85	8	0					100
5	0	27	6	0					120
6	40	57	7	33				99	
7	33	81	8	25				75	
8	25	48	7	18	86	6	100	54	
9	18	67	7	11				33	
10	11	52	7	4				12	
11	4	23	6	0					40
12	0	11	7	0					100
13	0	59	5	0					140
14	40	3	5	35				105	
15	35	3	5	30				90	
16	30	74	8	22				66	
17	22	64	7	15	40	4	100	45	
18	15	70	8	7				21	
19	7	43	7	0					0
20	0	87	8	0					160
Total Cost							300	696	660

18. The random number intervals are determined in the first place as shown in table 1 and 2

Table 1 Random Number Intervals (rained previously)

Event	Probability	Cum. Probability	Random Number Interval
No rain	.50	.5	00-49
1 cm rain	.25	.75	50-74
2 cm rain	.15	.90	75-89
3 cm rain	.05	.95	90-94
4 cm rain	.03	.98	95-97
5 cm rain	.02	1.00	98-99

Table 2 Random Number Intervals (No. Rain previously)

Event	Probability	Cum. Probability	Random Number Interval
No rain	.75	.75	00-74
1 cm rain	.15	.90	75-89
2 cm rain	.06	.96	90-95
3 cm rain	.04	1.00	96-99

The rainfall can now be predicted in accordance with the random number generated

Table 3: Simulation Worksheet

Day	Random Numbers	Rainfall (cm)	Table References
1	76	1	Table 2
2	78	2	Table 1
3	84	2	Table 1
4	75	2	Table 1
5	02	No rain	Table 1
6	86	1	Table 2
7	02	No rain	Table 1
8	78	1	Table 2
9	07	No rain	Table 1
10	63	No rain	Table 2

Total days without rain are 4 and total rain is 9 cm

19. Using the information that the factory works effectively 7 hours (= 420 minutes) a day, and the time required by each operator for producing each of the products, we obtain the following production and profit matrices:

Production Matrix (units)				
Operator	Product			
	A	B	C	D
P	70	42	30	35
Q	60	84	140	105
R	70	60	42	42
S	21	42	28	28

Profit Matrix (in Rs)				
Operator	Product			
	A	B	C	D
P	210	84	120	35
Q	180	168	560	105
R	210	120	168	42
S	63	84	112	28

In order to apply the assignment algorithm for minimising losses, let us first convert this profit matrix to a loss matrix by subtracting all the elements of the given matrix from its highest element which is equal to Rs. 560. The matrix so obtained is given below:

Operator	Product			
	A	B	C	D
P	350	476	440	525
Q	380	392	0	455
R	350	440	392	518
S	497	476	448	532

Now apply the assignment algorithm to the above loss matrix. Subtracting the minimum element of each row from all elements of that row, we get the following matrix:

Operator	Product			
	A	B	C	D
P	0	126	90	175
Q	380	392	0	455
R	0	90	42	168
S	49	28	0	84

Now subtract the minimum element of each column from all the elements of that column to get the following matrix:

Operator	Product			
	A	B	C	D
P	0	98	90	91
Q	380	364	0	371
R	0	62	42	84
S	49	0	0	0

Draw the minimum number of lines to cover all zeros. The minimum number of lines to cover all zeros is three which is less than the order of the square matrix (i.e. 4), thus the above matrix will not give the optimal solution. Subtract the minimum uncovered element (=62) from all uncovered elements and add it to the elements lying on the intersection of two lines, we get the following matrix:

Operator	Product			
	A	B	C	D
P	0	36	90	29
Q	380	302	0	309
R	0	0	42	22
S	111	0	62	0

The minimum number of lines which cover all zeros is 4 which is equal to the order of the matrix, hence, the above matrix will give the optimal solution. Specific assignments in this case are as below:

Operator	Product			
	A	B	C	D
P	0	36	90	29
Q	380	302	0	309
R	X	0	42	22
S	111	X	62	0

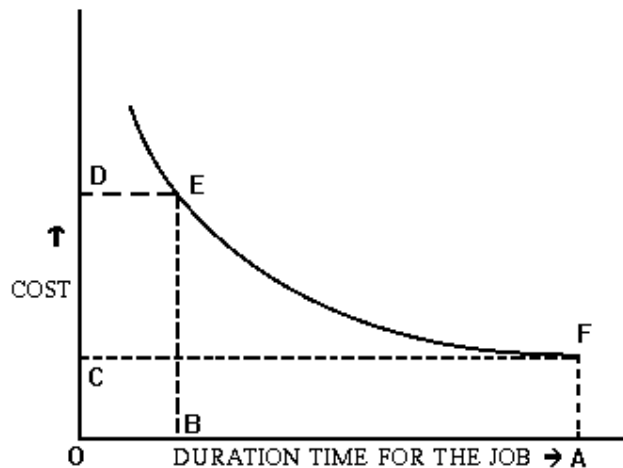
Operator	Product	Profit (Rs.)
P	A	210
Q	C	560
R	B	120
S	D	28
Total	Profit (Rs.)	918

20. (a) Project crashing using network analysis: In many situations, there may be compelling reasons to complete the project earlier than the originally estimated duration of the critical path on the basis of normal activity times. Or, in many cases, the execution of project gets

delayed due to certain reasons, we have to reduce the duration of future activities so that the project is completed earlier / or as per schedule. Under these circumstances, additional resources can be used to expedite certain activities resulting in earlier completion of the project. This shortening of activity times, which usually can be achieved by adding resources such as manpower or overtime is referred to as crashing the activity times. However, since the additional resources associated with crashing activity times usually result in added costs, the management would want to identify the least cost activities to crash and the amount of duration by which activities may be crashed to meet the desired project completion date.

In order to determine just where and how much to crash activity times, management would need following information:

1. Normal cost (N_c): This is the lowest possible direct cost required to complete an activity
2. Normal time (N_t): This is the minimum time required to complete an activity at normal cost.
3. Crash time (C_t): The minimum possible time in which an activity can be completed using additional resources.
4. Crash cost (C_c): The direct cost that is anticipated in completing an activity within the crash time.
5. Activity cost slope: A necessary measure for the cost analysis is the calculation of the cost slope for each activity. The cost slope indicates the additional cost incurred per unit of time saved in reducing the duration of an activity. It can be understood more clearly by considering the following diagram:



Let OA represent the normal time duration for completing a job and OC the normal cost involved to complete the job. Assume that the management wishes to reduce the time of completing the job to OB from normal time OA . Therefore, under such a situation the cost of the project increases and it goes up to say OD (Crash Cost). This only amounts to saying that by reducing the time period by AB the cost has increased by the amount CD . The rate of increase in the cost of activity per unit with a decrease in time is known as cost slope and is described as below:

$$\begin{aligned} \text{Activity cost slope} &= \frac{CD}{AB} = \frac{OD - OC}{OA - OB} \\ &= \frac{\text{Crash Cost} - \text{Normal Cost}}{\text{Normal Time} - \text{Crash Time}} \end{aligned}$$

Since the project duration is determined by the length of the critical path, it can be shortened by reducing the time of critical activities. As the objective of the management is to reduce

the project duration at the lowest possible cost, the critical activity with the lowest cost slope is selected for crashing. The amount of time by which an individual activity can be reduced is limited by its crash time. However, during such a crashing other factors must be taken into account. For example, the next longest route may also become critical. There will be then two critical paths and any further reduction in project time must occur on both the paths for overall project time to be reduced. The process is continued in this manner and the sum of direct and indirect costs i.e. the total costs for each completion time are tabulated. The optimum schedule corresponds to minimum total cost.

(b) Limitations of Linear Programming: Important limitations of linear programming problems are as follows:

- (i) A primary requirement of linear programming is that the objective function and every constraint function must be linear. This requires that the measure of effectiveness and resource usage must be proportional to the level of each activity conducted individually. However, programming problems which are non-linear arise quite frequently. It is occasionally possible to reformulate a non-linear programming problem into the linear programming format so that the simplex method can be used. This, however, is the fortunate exception rather than the rule.
- (ii) It may not be possible to solve those problems using linear programming in which non-linearity arises because of joint interactions between some of the activities regarding the total measure of effectiveness or total usage of some resource. Hence, linear programming problem requires that the total measure of effectiveness and total resource usage resulting from the joint performance of the activities must equal the respective sums of these quantities resulting from each activity being performed individually.

In some situations, it may not be true. For example, consider a situation where a by-product is produced with the scrap material from two primary products. The material would still have to be procured if only one of the two products were produced. However, the total material requirements if both products are produced is less than the sum of requirements if each were produced individually. It may not be possible to handle such situations with linear programming problems.

- (iii) In linear programming problem, fractional values are permitted for the decision variables. However, many decision problems require that the solution for decision variables should be obtained in non-fractional values. Rounding-off the values obtained by linear programming techniques may not result into an optimal solution in such cases.
- (iv) In linear programming problems, coefficients in the objective function and the constraint equations must be completely known and they should not change during the period of study i.e. they should be known constraints. In practical situation, it may not be possible to state all coefficients in the objective function and constraints with certainty. Furthermore, these coefficients may actually be random variables, each with an underlying probability distribution for the values. Such problems cannot be solved using linear programming.

PAPER – 6 : MANAGEMENT INFORMATION AND CONTROL SYSTEMS

QUESTIONS

1. Define the following terms:

(a) Open and Closed System	(b) Batch Processing
(c) Data Dictionary	(d) Mnemonic Codes
(e) Top Down Approach	(f) User Interface
(g) System Flow Chart	(h) DBMS
(i) Object Oriented Programming	(j) Unauthorised Intrusion
(k) Biometric Devices	(l) Logic Bomb or Worm
(m) SAP	(n) Significant Digit Subset Code
(o) Firewall	(p) Cross Compiler
(q) Piggybacking	(r) Distributed System
(s) Multi level Password Control.	
2. (a) What are the major differences between the System and Sub-System. Explain it with suitable example.
 (b) How an Information can be useful in business process. Explain.
 (c) What is Information System? Explain various categories of Information System.
3. (a) What are the different components of the Transaction Processing System?
 (b) How an Information can be required at different level of management through MIS.
 (c) What are the Advantages and Disadvantages of using MIS into the businesses?
4. (a) What are the different benefits by using MIS for decision making?
 (b) Explain the significance of DSS in today's business environment with an example.
 (c) What is EIS? How it is differ from MIS.
5. (a) Explain the component architecture of the Client/Server Technology.
 (b) Describes the benefit of using Client/Server Architecture over other computing model.
6. (a) What is SDLC? Explain each phase of SDLC in brief.
 (b) What is Prototyping? Describe the Advantages and Disadvantages of the Prototyping
 (c) Describe the various types of Feasibility Study that is used to develop new system.
7. (a) How DFD could be a tool for develop/design the data flow in a system. Explain it with a suitable example.
 (b) What are the various Fact Finding Techniques used in system design.
8. (a) What do you mean by System Design? What are the various issues which affect the output design of the system.
 (b) How a Data Communication and Storage affect the system design? Explain in brief.
9. (a) What are the various steps used to select the Software and Hardware in system acquisition process?
 (b) Describe in brief the methods to validate RFP in System Acquisition Process.
10. (a) How a program design tool is useful in software development process. Explain in brief.
 (b) Differentiate between the Testing and Debugging. What are the steps involved in system level testing.

11. (a) Describe the strategies to convert the existing system to the new system?
(b) How an evaluation system keep track to performed the new system in well manner? Describe in brief.
12. (a) Draw the system flow chart for a Production Scheduling System and explain the design factor involved in the system.
(b) Draw the system flow chart for a work-in-progress control and explain the design factor involved in the system.
13. (a) How an ERP is important to an organization? Describe the implementation of the ERP package in short.
(b) Write a short notes on BPR (Business Process Re-Engineering).
14. (a) What do you mean by General Control? What are the different component used to secure the OS.
(b) What are the Back-up and Recovery features necessary in a DBMS? Describe in brief.
(c) How Subversive Threats can be controlled using different techniques? Describe in brief.
15. (a) Describe the different categories of the processing control in brief.
(b) Describe the various checks that is used to validate the input data.
16. (a) What do you mean by Computer Fraud? Define different categories of the Computer Fraud.
(b) What are the different measurements that can reduce the potential for fraud.
(c) What are different techniques to detect the computer fraud.
17. (a) What is Cyber Law and Information Technology Act 2000. State the objectives of this Act.
(b) Describe each Chapter/Act of the Information Technology Act in brief.
18. (a) Describe the different concurrent audit techniques in brief.
(b) Describe the roles and the objectives of IS Auditor.
19. (a) Why Information Security is important to an organization? Discuss the various principles of the Information Security in brief.
(b) How an information be protected from Unauthorized Access? Discuss in brief.
20. (a) Describe the various integration of case tools available in the system. Describe in brief.
(b) What is Case Workbenches? Describe Analysis and Design workbenches.
21. Define the following:

(i) Ratio Analysis	(ii) Meta-case workbenches
(iii) Digital Signature	(iv) Check Digit
(v) Integrated Enterprises Management	(vi) Encryption
(vii) Client/Server Security	(viii) Hash Function
(ix) File Sharing Architecture	(x) Virus

SUGGESTED ANSWERS/HINTS

1. Define the following terms:
 - (a) Open and Closed system: A Closed System is self contained and does not interact or make exchange across its boundaries with its environment. Open System actively interact with other systems and establish exchange relationship. They exchange information, material or energy with the environment including random and undefined inputs.

- (b) **Batch Processing:** is the execution of a series of programs ("jobs") on a computer without human interaction, when possible. Batch jobs are set up so they can be run to completion without human interaction,.
- (c) **Data Dictionary:** is a set of metadata that contains definitions and representations of data elements. The simplest definition of metadata is that it is data about data. Metadata is information (data) about a particular content (data).
- (d) **Mnemonic Codes:** These are suitable where the codes have to be remembered by people e.g., BL. may stand for bolts. Mnemonics rely not only on repetition to remember facts, but also on associations between easy-to-remember information and to be remembered lists of data, based on the principle that the human mind much more easily remembers data attached to spatial, personal, or otherwise meaningful information than that occurring in meaningless sequences.
- (e) **Top Down Approach:** The top down approach assumes a high degree of top management involvement in the planning process and focuses on organisational goals, objectives and strategies.
- (f) **User Interface:** The user interface is the aggregate of means by which people (the users) interact with a particular machine, device, computer program or other complex tool (the system).
- (g) **System Flow Chart:** It is a graphic diagramming tool that documents and communicates the flow of data media and information processing procedures taking place in an information system.
- (h) **DBMS:** In computing, the computer program used to manage and query a database is known as a database management system (DBMS). The properties and design of database systems are included in the study of information science.
- (i) **Object Oriented Programming: (OOP)** is a programming paradigm that uses "objects" to design applications and computer programs. It uses several techniques from previously established paradigms, including inheritance, modularity, polymorphism, and encapsulation.
- (j) **Unauthorised Intrusion:** The intruder physically may enter the installation to steal assets or carry out sabotage. Alternatively, the intruder may eavesdrop on the installation by wire-tapping, installing an electronic bug or using a receiver that picks up electro-magnetic signals.
- (k) **Biometric Devices:** The ultimate in user authentication procedures is the use of biometric devices, which measure various personal characteristics, such as fingerprints, voice prints, retina prints, or signature characteristics. These user characteristics are digitized and stored permanently in a database security file or on an identification card that the user carries.
- (l) **Logic Bomb and Worm:** A logic bomb is a destructive program, such as a virus, that is triggered by some predetermined event. The term worm is used interchangeably with virus. A worm is a software program that "burrows" into the computer's memory and replicates itself into areas of idle memory.
- (m) **SAP:** is a business plan that has been created in the ERP system and it is a efficient tools that are available to assist, the actual results can be compared to planned ones and dimensions and ratios of interest can be found out for analysis purpose.
- (n) **Significant Digit Subset Code:** A well-conceived coding scheme, using significant-digit subset codes, can provide a wealth of information to users and management. Codes can be divided into subsets or subcodes, characters that are part of the identification number and that have special meaning.
- (o) **Firewall:** A firewall is a hardware or software device which is configured to permit, deny or proxy data through a computer network which has different levels of trust.
- (p) **Cross Compiler:** These are language processing systems which execute on the host machine and generate code for the target machine.

- (q) Piggybacking: Tapping into a telecommunications line and latching on to a legitimate user before he logs into the system; legitimate user unknowingly carries perpetrator into the system
 - (r) Distributed System: is a method of computer processing in which different parts of a program run simultaneously on two or more computers that are communicating with each other over a network.
 - (s) Multi Level Password Control: It is used to restrict employees who are sharing the same computers to specific directories, programs, and data files
2. (a) System (from Latin systēma) is a set of entities, real or abstract, comprising a whole where each component interacts with or is related to at least one other component and they all serve a common objective. The system may be defined as a set of interrelated elements that operate collectively to accomplish some common purpose or goal. A business is also a system where economic resources such as people, money, material, machines, etc are transformed by various organizational processes (such as production, marketing, finance etc.) into goods and services. A computer based information system is also a system which is a collection of people, hardware, software, data and procedures that interact to provide timely information to authorized people who need it. A general models of a physical system is input, process and output.

Subsystem is a set of elements, which is a system itself, and a part of the whole system. Each system is composed of subsystems, which in turn are made up of other subsystems, each sub-system being delineated by its boundaries. The interconnections and interactions between the subsystems are termed interfaces. Interfaces occur at the boundary and take the form of inputs and outputs. For Example in telecommunication, a communications subsystem is a functional unit which is smaller than the larger assembly under consideration subsystems.

For more details of the above points, students are advised to refer to the study material, Chapter-1, Section 1.1.

- (b) Information is the result of processing, manipulating and organizing data in a way that adds to the knowledge of the receiver. In other words, it is the context in which data is taken. Information as a concept bears a diversity of meanings, from everyday usage to technical settings. Generally speaking, the concept of information is closely related to notions of constraint, communication, control, data, form, instruction, knowledge, meaning, mental stimulus, pattern, perception, and representation. Information is data that have been put into a meaningful and useful context.

The term “data” and ‘information’ are often used interchangeably. However, the relation of data to information is that of raw material to finished product. A data processing system processes data to generate information. Information is the substance on which business decisions are based.

For more details of the above points, students are advised to refer to the study material, Chapter-1, Section 1.5.

- (c) An information system is the system that governs the information technology development, use, application and influence on a business or corporation. An information system, following a definition of Langefors[1], is a technologically implemented medium for recording, storing, and disseminating linguistic expressions, as well as for drawing conclusions from such expressions. Information systems are also social systems whose behavior is heavily influenced by the goals, values and beliefs of individuals and groups, as well as the performance of the technology.[2] Ciborra (2002) defines the study of information systems as the study that “deals with the deployment of information technology in organizations, institutions, and society at large.”

The different types of information systems are:

1. Transaction Processing Systems

2. Management Information Systems
3. Decision Support Systems
4. Executive Information Systems
5. Expert Systems

For more details of the above points, students are advised to refer to the study material Chapter-1, Section 1.6 and web link, http://en.wikipedia.org/wiki/information_system.

3. (a) A transaction processing system (TPS) is a type of information system that collect, store, modify, and retrieve the transactions of an organization. a transaction is an event that generates or modifies data that is eventually stored in an information system. the effective transaction processing systems ensure the capture of appropriate data and accurate information reporting. A transaction processing cycle consists of one or more application systems. Application system processes logically related transactions. The principal components of a transaction processing system include inputs, processing, storage, and outputs. These components or elements are part of both manual and computerized systems.

Inputs: Source documents, such as customer orders, sales slips, invoices, purchase orders, and employee time cards, are the physical evidence of inputs into the transaction processing system.

Processing: Processing involves the use of journals and registers to provide a permanent and chronological record of inputs.

Storage: Ledgers and files provide storage of data in both manual and computersied systems.

Outputs: There are a wide variety of outputs from a transaction processing system. Any document generated in the system is an output. Some documents are both output and input (e.g., a customer invoice is an output from the order-entry application system and also an input document to the customer). Other common outputs of a transaction processing system are the trial balance, financial reports, operational reports, pay cheques, bills of lading, and voucher cheques (payments to vendors).

- (b) MIS consists of three terms viz. management, information and system..



Management: refers to a set of functions and processes designed to initiate and co-ordinate group efforts in an organised setting directed towards promotion of certain interest, preserving certain values and pursuing certain goals. It involves mobilisation, combination, allocation and utilisation of physical, human and other needed resources in a judicious manner by employing appropriate skills, approaches and techniques.

Information: Information is data that have been put into a meaningful and useful context.

System: System may be defined as a composite entity consisting of a number of elements which are interdependent and interacting, operating together for the accomplishment of an objective.

Levels of management

- (i) **Top level (Strategic level):** Top management is defined as a set of management positions which are concerned with the overall task designing, directing and managing the organisation in an integrated manner.
- (ii) **Middle Level (tactical level):** Middle management is defined as a group of

management position which tend to overlap the top and supervisory management levels in the hierarchy. Middle management positions consist of heads of functional departments and chiefs of technical staff and service units.

- (iii) Supervisory level: Supervisory management is defined as a team of management positions at the base of the hierarchy. It consists of Section Officers, Office Managers and Superintendents, Foreman and supervisors who are directly responsible for instructing and supervising the efforts of clerical and 'blue collar' employees and workers.

(c) Advantages of MIS

1. Speed of processing and retrieval of data increases
2. Scope of use of information system has expanded
3. Scope of analysis widened
4. Complexity of system design and operation increased
5. Integrates the working of different information sub-system
6. Increases the effectiveness of Information system
7. More comprehensive information.

Disadvantages of MIS

1. MIS is not a substitute for effective management.
2. MIS may not have requisite flexibility to quickly update itself with the changing needs of time, especially in fast changing and complex environment.
3. MIS cannot provide tailor-made information packages suitable for the purpose of every type of decision made by executives.
4. MIS takes into account mainly quantitative factors, thus it ignores the non-quantitative factors like morale and attitude of members of the organisation, which have an important bearing on the decision making process of executives.
5. MIS is less useful for making non-programmed decisions.
6. The effectiveness of MIS is reduced in organisations, where the culture of hoarding information and not sharing with other holds.
7. MIS effectiveness decreases due to frequent changes in top management, organisational structure and operational team.

4. (a) Decision-Making as a managerial process and function of choosing a particular course of action out of several alternative courses for the purpose of achieving the given goals. It involves committing the organisation to specific courses of action and entails commitment of resources in specified ways. decision-making underlies much of managerial activity in organisations; decisions may be major or minor, strategic or operational. It is through making decisions and getting them implemented that managers strive to achieve organisational goals. There are several benefit by using MIS in decision making.

1. Makes a fairly accurate forecast of net income for one year.
2. Prepares short-term profit plans and long-range projections.
3. Provides preplanning information in budget preparation.
4. Calculates variances between budgeted and actual results.
5. Triggers revised forecasts if not proceeding in accordance with plan.
6. Acts as early warning system for monitoring activities and signaling necessary reactive plans.
7. Indicates effect on income and cash flow by following alternative investment strategies.

8. Assists in planning the addition of new facilities and a host of special studies.
 9. Accomplishes all the preceding items with great speed.
- (b) A Decision Support System (DSS) can be defined as a system that provides tools to managers to assist them in solving semi structured and unstructured problems in their own, somewhat personalized, way. A DSS is not intended to make decisions for managers, but rather to provide managers with a set of capabilities that enables them to generate the information required by them in making decisions. In other words, a DSS supports the human decision-making process, rather than providing a means to replace it.

Significance of DSS

- (1) They support semistructured or unstructured decision-making.
- (2) They are flexible enough to respond to the changing needs of decision makers, and
- (3) They are easy to use.

Some of the examples is Clinical Decision Support System for medical diagnosis. Other examples include a bank loan officer verifying the credit of a loan applicant or an engineering firm that has bids on several projects and wants to know if they can be competitive with their costs.

DSS is extensively used in business and management. Executive dashboard and other business performance software allow faster decision making, identification of negative trends, and better allocation of business resources.

For more details of the above points, students are advised to refer to the study material Chapter-5, Section 5.2 and web link, http://en.wikipedia.org/wiki/Decision_support_system

- (c) An Executive Information System (EIS) is a tool that provides direct on-line access to relevant information in a useful and navigable format. Relevant information is timely, accurate, and actionable information about aspects of a business that are of particular interest to the senior manager. The useful and navigable format of the system means that it is specifically designed to be used by individuals with limited time, limited keyboarding skills, and little direct experience with computers. An EIS is easy to navigate so that managers can identify broad strategic issues, and then explore the information to find the root causes of those issues.

Executive Information Systems differ from traditional information systems in the following ways:

- They are specifically tailored to executive's information needs.
 - They are able to access data about specific issues and problems as well as aggregate reports.
 - They provide extensive on-line analysis tools including trend analysis, exception reporting.
 - They can access a broad range of internal and external data.
 - They are particularly easy to use (typically mouse or touch-screen driven).
 - They are used directly by executives without assistance.
 - Screen-based - All EISs are delivered through terminals using easy-to-use software.
 - Information tends to be presented by pictorial or graphical means.
 - Information is presented in summary format, e.g. sales for the whole company.
 - The ability to manipulate data, to project 'what if' outcomes and to work with modeling tools within the system are also evident in EIS.
5. (a) Client/Server (C/S) refers to computing technologies in which the hardware and software components (i.e., clients and servers) are distributed across a network. The client/server

software architecture is a versatile, message-based and modular infrastructure that is intended to improve usability, flexibility, interoperability, and scalability as compared to centralised, mainframe, time sharing computing. This technology includes both the traditional database-oriented C/S technology, as well as more recent general distributed computing technologies.

Components of Client Server Architecture

Client: Clients, which are typically PCs, are the “users” of the services offered by the servers. There are basically three types of clients.

- Non-Graphical User Interface (NGUI)
- GUI-Clients
- Object-Oriented User Interface (OOUI)

Server: Servers await requests from the client and regulate access to shared resources. File servers make it possible to share files across a network by maintaining a shared library of documents, data, and images.

Middleware: The network system implemented within the client/server technology is commonly called by the computer industry as middleware. Middleware is all the distributed software needed to allow clients and servers to interact.

Network: The network hardware is the cabling, the communication cords, and the device that link the server and the clients. The communication and data flow over the network is managed and maintained by network software.

- (b) Client/server is described as a ‘cost-reduction’ technology. This technology allows doing what one may be currently doing with computers much less expensively. These technologies include client/server computing, open systems, fourth generation languages, and relational databases. Cost reductions are usually quoted as the chief reasons for changing to client/server.

Benefits of the Client /Server Technology

- Users are more productive today because they have easy access to data and because applications can be divided among many different users so efficiency is at its highest.
- Client/server applications make organizations more effective by allowing them to port applications simply and efficiently.
- Reduce the cost of the client’s computer: the server stores data for the clients rather than clients needing large amounts of disk space. Therefore, the less expensive network computers can be used instead.
- Reduce the cost of purchasing, installing, and upgrading software programs and applications on each client’s machine: delivery and maintenance would be from one central point, the server.
- The management control over the organization would be increased.
- Many times easier to implement client/server than change a legacy application.
- Leads to new technology and the move to rapid application development such as object oriented technology.
- Long term cost benefits for development and support.
- Easy to add new hardware to support new systems such as document imaging and video teleconferencing which would not be feasible or cost efficient in a mainframe environment.
- Can implement multiple vendor software tools for each application.

6. (a) Systems Development refers to the process of examining a business situation with the intent of improving it through better procedures and methods. Systems development can generally be thought of as having two major components: Systems Analysis and Systems Design. Systems Design is the process of planning a new business system or one to replace or complement an existing system. Systems Analysis, then, is the process of gathering and interpreting facts, diagnosing problems, and using the information to recommend improvements to the system. This is the job of the System Analyst.

SDLC is used by a systems analyst to develop an information system, including requirements, validation, training, and user ownership through investigation, analysis, design, implementation, and maintenance. The system development life cycle method can be thought of as a set of activities that analysts, designers and users carry out to develop and implement an information system.

The systems development life cycle method consists of the following activities:

- (i) Preliminary investigation
 - (ii) Requirements analysis or systems analysis
 - (iii) Design of system
 - (iv) Development of software
 - (v) Systems testing
 - (vi) Implementation and maintenance
- (b) Prototyping is the process of quickly putting together a working model (a prototype) in order to test various aspects of a design, illustrate ideas or features and gather early user feedback. Prototyping is often treated as an integral part of the system design process, where it is believed to reduce project risk and cost. Often one or more prototypes are made in a process of incremental development where each prototype is influenced by the performance of previous designs, in this way problems or deficiencies in design can be corrected. When the prototype is sufficiently refined and meets the functionality, robustness, manufacturability and other design goals, the product is ready for production.

The goal of prototyping approach is to develop a small or pilot version called a prototype of part or all of a system. A prototype is a usable system or system component that is built quickly and at a lesser cost, and with the intention of being modifying or replacing it by a full-scale and fully operational system. When a prototype is developed that satisfies all user requirements, either it is refined and turned into the final system or it is scrapped. If it is scrapped, the knowledge gained from building the prototype is used to develop the real system.

Advantages of prototyping

- May provide the proof of concept necessary to attract funding
- Early visibility of the prototype gives users an idea of what the final system looks like
- Encourages active participation among users and producer
- Enables a higher output for user
- Cost effective (Development costs reduced)
- Increases system development speed
- Assists to identify any problems with the efficacy of earlier design, requirements analysis and coding activities
- Helps to refine the potential risks associated with the delivery of the system being developed

Disadvantages of prototyping

- User's expectation on prototype may be above its performance
- Possibility of causing systems to be left unfinished
- Possibility of implementing systems before they are ready
- Producer might produce a system inadequate for overall organization needs
- Producer might get too attached to it (might cause legal involvement)
- Often lack flexibility
- Not suitable for large applications
- Project management difficulties

For more details of the above points, students are advised to refer to the study material Chapter-7, Section 7.2.2 and web link <http://en.wikipedia.org/wiki/Prototyping>

- (c) Feasibility Study refers to a process of evaluating alternative systems through cost/benefit analysis so that the most feasible and desirable system can be selected for development. The feasibility study of a system is undertaken from three angles: technical, economic and operational feasibility.

Technical feasibility: It is concerned with hardware and software. Essentially, the analyst ascertains whether the proposed system is feasible with existing or expected computer hardware and software technology.

Economic feasibility: It includes an evaluation of all the incremental costs and benefits expected if the proposed system is implemented. This is the most difficult aspect of the study.

Operational feasibility: It is concerned with ascertaining the views of workers, employees, customers and suppliers about the use of computer facility. The support or lack of support that the firm's employees are likely to give to the system is a critical aspect of feasibility.

Some of the other feasibilities are as follows:

Schedule Feasibility: Schedule feasibility involves the design team's estimating how long it will take a new or revised system to become operational and communicating this information to the steering committee.

Legal Feasibility: Legal feasibility is largely concerned with whether there will be any conflict between a newly proposed system and the organization's legal obligations.

7. (a) A Data Flow Diagram (DFD) graphically describes the flow of data within an organization. a flow diagram can also be used for the visualization of data processing (structured design). It is used to document existing systems and to plan and design new ones.

A DFD is composed of four basic elements: data sources and destinations, data flows, transformation processes, and data stores.

Symbol	Name	Explanation
	Data Sources and destinations	The people and organizations that send data to and receive data from the system are represented by square boxes. Data destinations are also referred to as data sinks.
	Data flows	The flow of data into or out of a process is represented by curved or straight lines with arrows.

	Transformation process	The processes that transform data from inputs to outputs are represented by circles. They are often referred to as bubbles.
	Data stores	The storage of data is represented by two horizontal lines.

Data Flow Diagram Symbols

Subdividing the DFD

DFDs are subdivided into successively lower levels in order to provide ever-increasing amounts of detail, because few systems can be fully diagrammed on one sheet of paper. Since users have differing needs, a variety of levels can better satisfy these requirements. The highest-level DFD is referred to as a context diagram. A context diagram provides the reader with a summary-level view of a system. It depicts a data processing system as well as the external entities that are the sources and destinations of the system's inputs and outputs.

For more details of the above points, students are advised to refer to the study material, Chapter-7, Section 7.6 and http://en.wikipedia.org/wiki/Data_flow_diagram

- (b) Every system is built to meet some set of needs, for example, the need of the organisation for lower operational costs, better information for managers, smooth operations for users or better levels of service to customers. To assess these needs, the analysts often interact extensively with the people, who will be benefited from the system, in order to determine what are their actual requirements. Various fact-finding techniques, which are used by the system analyst for determining these needs/ requirements, are below:
1. Documents: Document means manuals, input forms, output forms, diagrams of how the current system works, organisation charts showing hierarchy of users and manager responsibilities, job descriptions for the people who work with the current system, procedure manuals, program codes for the applications associated with the current system, etc.
 2. Questionnaires: Users and managers are asked to complete questionnaire about the information system when the traditional system development approach is chosen. The main strength of questionnaires is that a large amount of data can be collected through a variety of users quickly. Also, if the questionnaire is skillfully drafted, responses can be analysed rapidly with the help of a computer.
 3. Interviews: Users and managers may also be interviewed to extract information in depth. The data gathered through interviews often provide systems developer with a complete picture of the problems and opportunities. Interviews also give analyst the opportunity to note user reaction first-hand and to probe for further information.
 4. Observation: In prototyping approaches, observation plays a central role in requirement analysis. Only by observing how users react to prototypes of a new system, the system can be successfully developed. The analyst should visit the user site to watch how the work was taking place. The value of observational visits by analyst can be great.
8. (a) Systems design is the process or art of defining the hardware and software architecture, components, modules, interfaces, and data for a computer system to satisfy specified requirements

The system design phase usually consists of following three activities:

- (i) Reviewing the system's informational and functional requirements;
- (ii) Developing a model of the new system, including logical and physical specifications of outputs, inputs, processing, storage, procedures and personnel;

(iii) Reporting results to management.

System design involves first logical design and then physical construction of a system. When analysts formulate a logical design, they write the detailed specifications for the new system, they describe its features; the outputs, input files, databases and procedures, all in a manner that meets systems requirements. The statement of these features is termed as the design specifications of the system.

Issues related with the output design of the system

The term output applies to any information produced by an information system, whether printed or displayed. System output may be a report, a document or a message. There are six important factors which should be considered by the system analyst while designing user outputs:

- (i) Content
- (ii) Form
- (iii) Output volume
- (iv) Timeliness
- (v) Media
- vi) Format.

For more details of the above points, students are advised to refer to the study material Chapter-8, Section 8.2 and web link http://en.wikipedia.org/wiki/system_design

- (b) Data Storage is often an important decision in the design of an information system. There are two approaches for storing data. The first approach is to store data in individual files, one file for each application. The second approach is to develop a database that can be shared by many users for a variety of applications as need arises.

The Conventional File Approach may at times be a more efficient approach since the file can be application oriented. On the other hand, the data base approach may be more appropriate because the same data need to be entered, stored and updated once. Examples of conventional files include master files, table files, transaction files, work files, and report files. They can have a sequential organization, random or direct organization, indexed organization, or indexed-sequential organization. These are the most effective ways of organizing and storing data in transaction systems where each transaction is processed to update a record in the master file.

In Data Communication Information Systems in practice involve the transmission of data between different locations. The systems analyst is responsible not only for selecting the right communication equipment, whether it is for large or small systems or whether transmission is over wide or limited areas, but also for the steps that must be taken to design the application, specifying the method for linking the application into the communication network and selecting the most useful and cost effective communication services.

Requirements for Data Communication System

The system analysts must select the following components:

1. For communications channels, he may have to make a decision regarding channel selection, transmission rate, leased or dial-up line, type of line, for example, simplex or half-duplex etc.
2. Communications control devices: The analyst is required to select devices such as modems, data service units, multiplexer and concentrator, data switches, etc. In addition the analyst may also select the type of network (LAN or WAN), network topology (point-to-point or multi drop) etc. and the network architecture to be utilized for the proposed project.

9. (a) Acquiring the appropriate hardware and software is critical for the success of the whole project. The organisation can discover new hardware and software developments in various ways. The selection of an appropriate computer system, both hardware and application software package demands a high level of expertise and many organisations use a consultant either to provide guidance to their personnel or to manage this activity. There are various steps for selection of the appropriate computer system.

1. Prepare the design specifications.
2. Prepare and distribute an RFP (Request for proposal) to selected computer vendors.
3. On the basis of an analysis of proposals, eliminate vendors whose proposals are inferior.
4. Have vendors present their proposals.
5. Conduct further analysis of the proposals.
6. Contact present users of the proposed systems.
7. Conduct equipment benchmark tests.
8. Select the equipment.

- (b) 3 Methods to validate the vendor proposal:

- (1) Checklists: It is the most simple and rather a subjective method for validation and evaluation. The various criteria are put in check list in the form of suitable questions against which the responses of the various vendors are validated.
 - (a) Software Validation Checklist
 - (b) Support Service Checklists.
- (2) Point-Scoring Analysis: Another approach for evaluating those accounting packages that meet most of a company's major requirements is a point-scoring analysis. (This analysis can also be used to evaluate hardware as well). When performing a point-scoring analysis, the evaluation committee first assigns potential points to each of the evaluation criteria based on its relative importance. Although point-scoring analyses provide an objective means of selecting a final system, many experts believe that evaluating accounting software is more of an art than science. There are no absolute rules in the selection process, only guidelines for matching user needs with software capabilities.
- (3) Public evaluation reports: Several consultancy agencies compare and contrast the hardware and software performance for various manufacturers and publish their reports in this regard. This method has been frequently and usefully employed by several buyers in the past. This method is particularly useful where the buying staff has inadequate knowledge of computer facts.

For more details of the above points, students are advised to refer to the study material, Chapter-9, Section 9.4.1.

10. (a) There are several design tools which are available to develop the program in well structured manner. They are:

1. Program Flow Chart: Program flow chart is among the most common program design tools that managers and users encounter when reviewing the design work of the system development project. These flow charts depict the logical steps through which a computer program must proceed when solving a problem. At one time, program flow charts were considered the premier program design tool. Although they are still widely used, sometimes it is difficult for programmers to translate a program flow chart directly into a structured code.
2. Pseudo Code: When reviewing the work done by a program designer, users may also need to review narrative descriptions of a program logic. Pseudocode, like program

flow charts, also represents program logic. However, instead of using graphical symbols and flow lines, pseudo code presents program logic in English - like statements.

3. **Structure Chart:** Another type of program design tool that a user may review is the program structure chart. Structure charts, which look similar to corporate organisation charts are useful for organising problems.
 4. **4GL Tools:** Fourth-generation languages provide a way out to remove these obstacles by automating many of these manual tasks by using 4GL tools. These tools ensure that the work done with them is consistent with the other work performed by the system team. The automation of manual task and internal consistency checks are two reasons due to which productivity gains result from using 4GL tools.
 5. **Object Oriented Programming and Design Tools:** These tools provide a means of enhancing programmer productivity and of reducing the application backlogs common in many organisations. Object oriented software design results in a model that describes object, classes and their relationships to one another. By adopting 4GL and object-oriented programming tools, the organisations can decrease their application development time substantially.
- (b) **Software Debugging** is a methodical process of finding and reducing the number of bugs, or defects, in a computer program or a piece of electronic hardware thus making it behave as expected. The process of debugging a program refers to correcting programming language syntax and diagnostic errors so that the program “compiles cleanly”. A clean compile means that the program can be successfully converted from the source code written by the programmer into machine language instructions. Debugging can be a tedious task. It consists of four steps: inputting the source program to the compiler, letting the compiler find errors in the program, correcting lines of code that are in error, and resubmitting the corrected source program as input to the compiler. The length of time required to debug a program can be shortened considerably by the use of an interactive compiler which checks the source program and displays any errors on a CRT or prints them on a printer.

Software testing is the process used to measure the quality of developed computer software such as capability, reliability, efficiency, portability, maintainability, compatibility, and usability. Testing is a process of technical investigation, performed on behalf of stakeholders, that is intended to reveal quality-related information about the product with respect to the context in which it is intended to operate. White box and black box testing are terms used to describe the point of view a test engineer takes when designing test cases. Black box being an external view of the test object and white box being an internal view.

System testing: in which the software is integrated to the overall product and tested to show that all requirements are met. System-level testing must be conducted prior to installation of an information system. It involves:

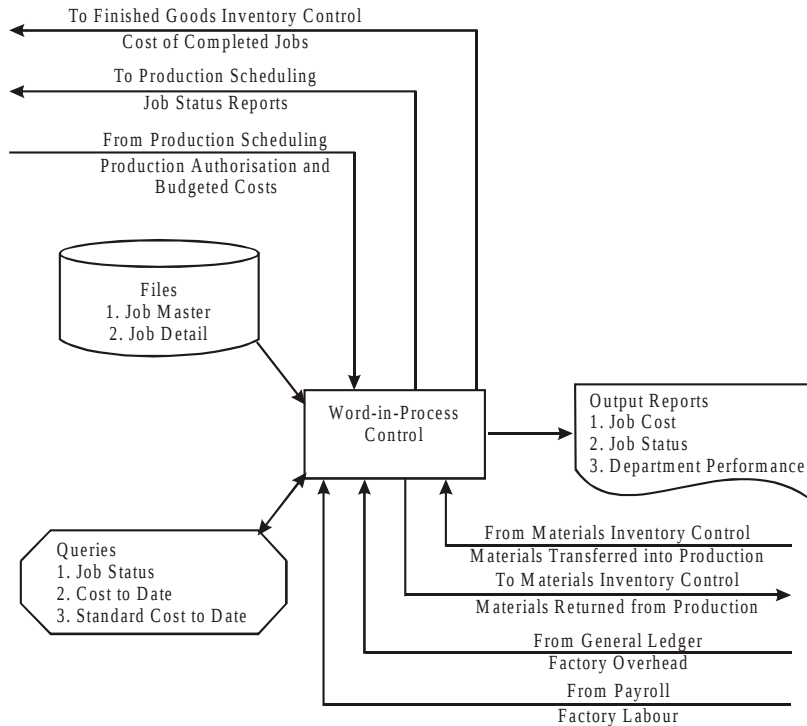
- (a) preparation of realistic test data in accordance with the system test plan,
- (b) processing the test data using the new equipment
- (c) thorough checking of the results of all system tests, and
- (d) reviewing the results with future users, operators and support personnel.

For more details of the above points, students are advised to refer to the study material Chapter-8, Section 8.2 and web link, <http://en.wikipedia.org/wiki/Debugging>, http://en.wikipedia.org/wiki/Software_testing#

11. (a) **Conversion or changeover** is the process of changing from the old system (manual system) to the new system. It requires careful planning to establish the basic approach to be used in the actual changeover. There are many conversion strategies available to the analyst who has to take into account several organizational variables in deciding which conversion strategy to use.

There are five strategies for converting from the old system to the new one:

1. Direct changeover: Conversion by direct changeover means that on a specified date, the old system is dropped and the new system is put into use. Direct changeover can only be successful if extensive testing is done beforehand.
 2. Parallel conversion: This refers to running the old system and the new system at the same time, in parallel. Both systems are run simultaneously for a specified period of time and the reliability of results is examined. When the same results are gained over time, the new system is put into use and the old one is stopped.
 3. Gradual conversion: Gradual conversion attempts to combine the best features of the earlier two plans, without incurring the risks. In this plan, the volume of transactions is gradually increased as the system is phased in.
 4. Modular prototype conversion: This approach to conversion uses the building of modular, operational prototypes to change from old systems to new in a gradual manner. As each module is modified and accepted, it is put into use.
 5. Distributed conversion: This refers to a situation in which many installations of the same system are contemplated, such as in banking or in franchises such as restaurants or clothing stores. One entire conversion is done (with any of the four approaches considered already) at one site. When that conversion is successfully completed, other conversions are done for other sites.
- (b) Evaluation provides the feedback necessary to assess the value of information and the performance of personnel and technology included in the newly designed system. There are two basic dimensions of information systems that should be evaluated. The first dimension is concerned with whether the newly developed system is operating properly. The other dimension is concerned with whether the user is satisfied with the information system with regard to the reports supplied by it.
- Development evaluation: Evaluation of the development process is primarily concerned with whether the system was developed on schedule and within budget. This is a rather straightforward evaluation.
 - Operation evaluation: The evaluation of the information system's operation pertains to whether the hardware, software and personnel are capable to perform their duties and they do actually perform them so.
 - Information evaluation: An information system should also be evaluated in terms of information it provides. This aspect of system evaluation is difficult and it cannot be conducted in a quantitative manner, as is the case with development and operation evaluations. The objective of an information system is to provide information to support the organizational decision system. Therefore, the extent to which information provided by the system is supportive to decision making is the area of concern in evaluating the system.
12. (a) The work-in-process control system assigns materials, labour, and overhead costs to production jobs or products. In a job-order system, each cost is assigned to a specific job. In a process costing system, costs are assigned to departments and then to products. The objectives of a work-in-process system are to cost jobs through the manufacturing process and provide management with information to assist in controlling cost and measuring the performance of departments or other units within the factory.



System Interfaces

The work-in-process control system interfaces directly with the payroll, general ledger, finished goods inventory control, production scheduling, and materials inventory control systems.

Labour cost distribution and factory overhead allocation are inputs from the payroll and the general ledger systems, respectively. Aggregate work-in-process inventory transferred to finished goods is sent from work-in-process control to the general ledger. The aggregate journal entry is:

Finished goods inventory control	XXXX
Work in process	XXXX

Once manufacturing is complete, jobs are transferred from work-in-process control to finished goods inventory control—that is, from the production management system to the marketing system.

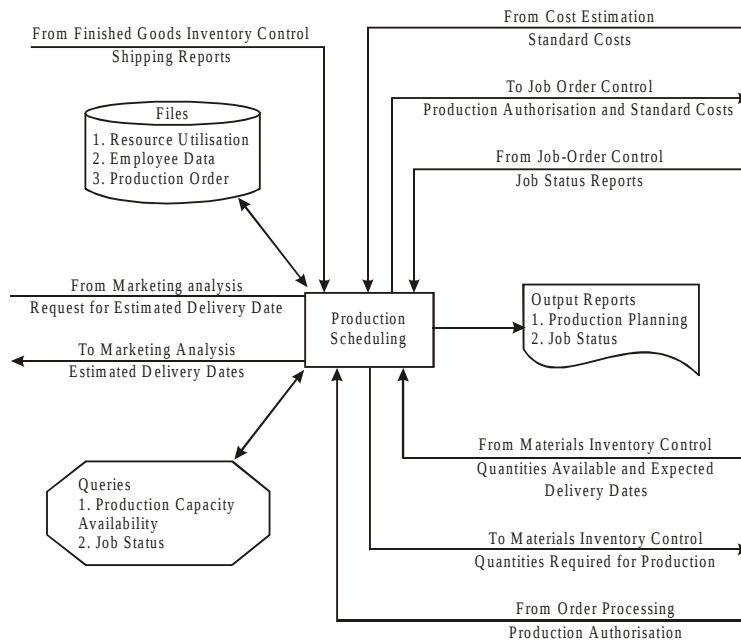
Files and Inputs

A typical work-in-process system in a manufacturing firm contains a job file that has one record for each job in the manufacturing process. The job detail file contains in-depth information about each job. When authorisation to start a job is received from production scheduling, a record is created for the job. A bill of materials, a machine schedule, and a labour schedule are entered into the file.

Reports

The work-in-process control system produces job cost, job status, and department performance reports periodically. A job cost report contains a detailed summary of the costs incurred to date, the budgeted cost, and estimated completion dates for each job in the system.

- (b) Production scheduling is the nerve centre of the production management system. It produces no general ledger journal entries, but it schedules production and monitors all physical flows.



System Interfaces

Within the production management system, the production scheduling and materials inventory control systems interface frequently. Production scheduling informs materials inventory control of the items and quantities required to schedule production, and inventory control indicates the quantities available. Work-in-process control receives production authorisation from the scheduling system. This authorisation creates a new record for a job, and production costs can be charged to the job. At the same time, the work-in-process control system receives the standard cost for the job and provides status reports to the scheduling system. Cost estimation provides production scheduling with budgeted standard costs for all jobs production.

Files and Inputs

Three files are required in the production scheduling system. The resource utilisation file contains a record for each machine and production process in the factory and maintains work schedules for them. The employee data file contains data concerning employee skills and scheduled work assignments. The production order file maintains completion dates and schedule information for each job.

Reports

The scheduling system produces periodic production planning reports. They indicate the available capacity and scheduled future utilisation of labour and machinery. Such reports are useful to management because they indicate where excess capacity exists for the planning period. Sales and pricing strategies can be considered to alleviate the situation.

13. (a) An Enterprise Resource Planning System is a fully integrated business management system covering functional areas of an enterprise like Logistics, Production, Finance, Accounting and Human Resources. It organizes and integrates operation processes and information flows to make optimum use of resources such as men, material, money and machine.

In simple words, Enterprise resource planning promises one database, one application, and one user interface for the entire enterprise, where once disparate systems ruled manufacturing, distribution, finance and sales.

ERP implementation is a special event in an organisation. It brings together in one platform, different business functions, different personalities, procedures, ideologies and philosophies with an aim to pool knowledge base to effectively integrate and bring worthwhile and beneficial changes throughout the organization. An ERP package after implementation is expected to improve the flow of information and formalize and standardize all the business processes and workflow that exist in an enterprise. However the workload of users may not decrease. It is worthwhile to remember that ERP is an enabling tool, which makes one do his work better, which naturally need additional efforts.

Several steps are involved in the implementation of a typical ERP package. These are:

1. Identifying the needs for implementing an ERP package.
2. Evaluating the 'As Is' situation of the business i.e., to understand the strength and weakness prevailing under the existing circumstances.
3. Deciding the 'Would be' situation for the business i.e., the changes expected after the implementation of ERP.
4. Reengineering the Business Process to achieve the desired results in the existing processes.
5. Evaluating the various available ERP packages to assess suitability.
6. Finalising of the most suitable ERP package for implementation.
7. Installing the required hardware and networks for the selected ERP package.
8. Finalising the Implementation consultants who will assist in implementation.
9. Implementing the ERP package.

For more details of the above points, students are advised to refer to the study material, Chapter-12, Section 12.1.5

- (b) BPR is a management approach aiming at improvements by means of elevating efficiency and effectiveness of the processes that exist within and across organizations. The key to BPR is for organizations to look at their business processes from a "clean slate" perspective and determine how they can best construct these processes to improve how they conduct business. Business process reengineering is also known as BPR, Business Process Redesign, Business Transformation, or Business Process Change Management.

Every company that intends to implement ERP has to reengineer its processes in one form or the other. This process is known as Business Process Reengineering (BPR).

The most accepted and formal definition for BPR, given by Hammer and Champy is reproduced here: "BPR is the fundamental rethinking and radical redesign of processes to achieve dramatic improvement, in critical, contemporary measures of performance such as cost, quality, service and speed,"

Business Engineering: Business Engineering is the rethinking of Business Processes to improve speed, quality and output of materials or services. The emphasis of business engineering is the concept of Process Oriented Business Solutions enhanced by the Client-Server computing in Information Technology. Business Engineering is the method of development of business processes according to changing requirements.

Business Management: ERP merges very well with common business management issues like Business Process Reengineering, total quality management, mass customization, service orientation, and virtual corporation etc. The first step in implementation of ERP is the development of a Business process model showing business process as one large system and the interconnection and sequence of business subsystems or processes that drive it.

For more details of the above points, students are advised to refer to the study material, Chapter-12, Section 12.2 and web link <http://en.wikipedia.org/wiki/BPR>

14. (a) Computer based Information internal controls are divided into following broad categories:

1. General controls: These controls apply to a wide range of exposures that systematically threaten the integrity of all applications processed within the Computer Based Information System (CBIS) environment.
2. Application Controls: These controls are focused on exposures associated with specific systems, such as payroll, accounts receivables, and so on.

Operating System Control : The Operating System is the computer's control program. It allows users and their applications to share and access common computer resources, such as processors, main memory, databases, and printers. The modern accountant needs to recognize the operating system's role in the overall control picture to properly assess the risks that threaten the accounting systems.

Operating System Security: Operating system security involves policy, procedures, and controls that determine who can access the operating system, which resources (files, programs, printers) they can access, and what actions they can take. The following security components are found in secure operating systems.

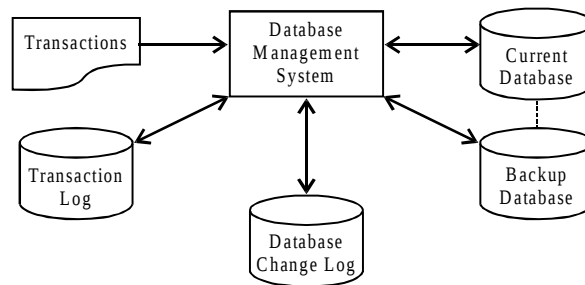
1. Log-On Procedure
2. Access Token
3. Access Control List
4. Discretionary Access Control.

(b) Controls over Data Management fall into two general categories: Access Controls and Backup Controls. Access controls are designed to prevent unauthorized individuals from viewing, retrieving, corrupting, or destroying the entity's data. Backup controls ensure that in the event of data loss due to unauthorized access, equipment failure, or physical disaster, the organisation can recover its files and databases.

Back-up and Recovery control: Data can be corrupted and destroyed by malicious acts from external hackers, disgruntled employees, disk failure, program errors, fires, floods, and earthquakes. To recover from such disasters, organizations must implement policies, procedures and techniques that systematically and routinely provide backup copies of critical files.

- (1) The file security: The techniques employed for reconstruction of master files on magnetic disks and tapes, in the event of their loss/destruction.
 - (a) Magnetic Disk: Contents of master file on magnetic disk are periodically copied or dumped on magnetic tape backup file and stored at another location
 - (b) Magnetic Tapes: The procedures followed in reconstruction of files in case of magnetic tapes is referred to as Generation Technique because files relating to two previous periods are retained in addition to the current updated master file and the current transaction file.
- (2) Backup Controls in the Database Environment: Since data sharing is a fundamental objective of the database approach, this environment is particularly vulnerable to damage from individual users. One unauthorized procedure, one malicious act, or one program error can deprive the entire user community of its information resource.

Database Backup and Recovery



Backup: The backup feature makes a periodic backup of the entire database. This is an automatic procedure that should be performed at least once a day. The backup copy should then be stored in a secure remote area.

Transaction Log (Journal): The transaction log feature provides an audit trail of all processed transactions. It lists transactions in a transaction log file and records the resulting changes to the database in a separate database change log.

Checkpoint Feature: The checkpoint facility suspends all data processing while the system reconciles the transaction log and the database change log against the database. **Recovery Module.** The recovery module uses the logs and backup files to restart the system after a failure.

- (c) An intruder attempts to violate the integrity of some components in the subsystem is known as subversive threats. Subversive attacks can provides intruders with important information about messages being transmitted. There are different techniques to control the subversive threats.
 - (a) Firewalls: Organisations connected to the Internet or other public networks often implement an electronic "firewall" to insulate their Intranet from outside intruders. A firewall is a system that enforces access control between two networks. Firewalls can be grouped into two general types: network-level firewalls, and application-level firewalls.
 1. Network-level firewalls
 2. Application-level firewalls
 - (b) Controlling Denial of Service Attacks: Computer hackers and crackers have devised a malicious act called a denial of service attack, in which the attacker transmits hundreds of SYN packets to the targeted receiver but never responds with an ACD to complete the connection. As a result, the ports of the receiver's server are clogged with incomplete communication requests that prevents legitimate transactions from being received and processed. Denial of service attacks can severely hamper an organisation's ability to use the Internet to conduct commerce.
 - (c) Encryption: Encryption is the conversion of data into a secret code for storage in databases and transmission over networks. The discussion here pertains to transmitted data, but these basic principles apply also to stored data. The sender uses an encryption algorithm to convert the original message called clear text into a coded equivalent called cipher text. At the receiving end, the cipher text is decoded (decrypted) back into clear text. The encryption algorithm uses a key, which is a binary number that is typically from 56 to 128 bits in length. Two general approaches to encryption are private key and public key encryption.
 1. Private Key Encryption

2. Public Key Encryption.

- (d) Message Transaction Log: An intruder may successfully penetrate the system by trying different password and user ID combinations. Therefore, all incoming and outgoing messages, as well as attempted (failed) access, should be recorded in a message transaction log.
- (e) Call Back Devices: A call-back device requires the dial-in user to enter a password and be identified. The system then breaks the connection to perform user authentication. If the caller is authorized, the call-back device dials the caller's number to establish a new connection.

15. (a) Application Controls deal with exposures within specific applications, such as payroll, purchases, and cash disbursements systems. Application controls, which may be manual actions or procedures programmed into an application, fall into three broad categories: input controls, processing controls, and output controls.

Processing controls are divided into three categories: run-to-run controls, operator intervention controls, and audit trail controls.

1. Run-to-Run Controls: Run-to-run controls use batch figures to monitor the batch as it moves from one programmed procedure (run) to another. These controls ensure that each run in the system processes the batch correctly and completely. Batch control figures may be contained in either a separate control record created at the data input stage or an internal label

- (a) Recalculate Control Totals
- (b) Transaction Codes
- (c) Sequence Checks

2. Operator Intervention controls: Systems sometimes require operator intervention to initiate certain actions, such as entering control totals for a batch of records, providing parameter values for logical operations, and activating a program from a different point when reentering semi-processed error records.

3. Audit Trail Controls: In an accounting system, every transaction must be traceable through each stage of processing from its economic source to its presentation in financial statements. In a Computer Based Information Systems (CBIS) environment, the audit trail can become fragmented and difficult to follow.

- (a) Transaction Logs
- (b) Transaction Listings
- (c) Log of Automatic Transaction
- (d) Listing of Automatic Transactions
- (e) Unique Transaction Identifiers
- (f) Error Listing

- (b) The data collection component of the information system is responsible for bringing data into the system for processing. Input controls at this stage attempt to ensure that these transactions are valid, accurate, and complete. Data input procedures can be either source document-triggered (batch) or direct input (real-time).

Input validation controls are intended to detect errors in transaction data before the data are processed. Validation procedures are most effective when they are performed as close to the source of the transaction as possible.

There are three levels of input validation controls:

- (a) Field interrogation
- (b) Record interrogation

- (c) File interrogation
 - (a) Field Interrogation: Field interrogation involves programmed procedures that examine the characters of the data in the field. The following are some common types of field interrogation.
 - (i) Limit checks: may be applied to both the input data and the output data. The field is checked by the program to ensure that its value lies within certain predefined limits (in the program).
 - (ii) Picture Checks: These check against entry into processing of incorrect characters.
 - (iii) Valid Code Checks: Checks are made against predetermined transactions codes, tables or order data to ensure that input data are valid.
 - (iv) Check Digit: A check digit is a control digit (or digits) added to the code when it is originally assigned that allows the integrity of the code to be established during subsequent processing.
 - (v) Arithmetic Checks: Arithmetic is performed in different ways to validate the result of other computations of the values of selected data fields.
 - (vi) Cross Checks: may be employed to verify fields appearing in different files to see that the result tally.
 - (b) Record interrogation
 - (i) Sequence checks are exercised to detect any missing transaction, off serially numbered vouchers (subsequently transcribed for computer processing) or erroneous sorting.
 - (ii) Format completeness checks are used to check the presence and position of all the fields in a transaction.
 - (iii) Redundant data checks are used in sequential processing. Matching keys of the transaction record and its master record may not be deemed enough.
 - (iv) Combination checks: Credit against shipments is invalid and ought to be rejected.
 - (v) Passwords are issued to the various users in on-line systems for processing their inquiries.
 - (c) File Interrogation: The purpose of file interrogation is to ensure that the correct file is being processed by the system.
 - (i) Internal label checks verify that the file processed is the one the program is actually calling for.
 - (ii) Version checks are used to verify that the version of the file being processed is correct.
 - (iii) An expiration date check prevents a file from being deleted before it expires.
16. (a) Fraud refers to any and all means a person uses to gain an unfair advantage over another person. Fraudulent acts include lies, suppression of truth, tricks, and they often involve a violation of a trust or confidence.

Computer frauds have been defined as any illegal act for which knowledge of computer technology is essential for its perpetration, investigation or prosecution. It might be generally thought that computer fraud means no more than "using a computer to commit fraud". This is far too narrow a definition in view of the many ways that businesses can face the risk of loss as a result of the use or misuse of a computer.

A more extensive definition of computer fraud could be as given below:

“Using a computer to cause prejudice, in the sense of financial and/or reputational damage, to a business” may be called a computer fraud.

- (a) Clearly recognizable frauds: Such as investment frauds, secret market frauds and pyramid schemes where a computer (usually via the Internet) is used as a new medium to convey an old message and the hapless victim is persuaded to part with money or credit card details
 - (b) Hacking: In the generally recognised sense of unauthorised access and unauthorised modification to computers. This includes the malicious introduction of a virus, the malicious modification of email or the vandalism of Web pages
 - (c) Manipulation of computer systems to obtain money from an employer or a third party: Examples of this are diversion of payments and creation of false employees/suppliers. These frauds may require access to a system or part of a system from which the perpetrator is (or is supposed to be) excluded.
 - (d) Theft and/or destruction of confidential and sensitive information: This is an area where huge damage can be caused by employees and third parties who are able to gain access to confidential and sensitive information and pass it on to competitors or simply destroy it;
 - (e) Abuse of computer systems by employees: This involves an employee using the computer system for his or her own purposes. Employees can write personal letters or run businesses from their employer's computers. Employees can use email systems and the Internet for private purposes
 - (f) Software Piracy: By either using counterfeit or unlicensed software or by distributing counterfeit software by disk, CD or through the Internet.
- (b) Because fraud is such a serious problem, organisations must take every precaution to protect their information systems. a number of measures can significantly decrease the potential for fraud and any resulting losses.
- (a) Make Fraud Less Likely to Occur: Some computer consultants claim that the most effective method of obtaining adequate system security is to rely on the integrity of company employees. Organizations can take steps to increase employee integrity and reduce the likelihood of employees committing a fraud.
 - (b) Use Proper Hiring and Firing Practices: A manager's most important responsibilities is to hire and retain honest people. Similarly, a company should be very careful when firing employees.
 - (c) Manage Disgruntled Employees: Many employees who commit fraud are seeking revenge or “justice” for some wrong they perceive has been done to them. Hence companies should have procedures for identifying these individuals and either helping them resolve their feelings or removing them from jobs with system access.
 - (d) Train Employees in Security and Fraud Prevention Measures: Employee training and education is the most important element of any security program. Fraud is much less likely to occur in an environment where employees believe security is everyone's business.
- (c) To reduce the risk to business from computer fraud, computer forensic tools can be used. These have a much wider application than just dealing with computer fraud. They can be applied in any investigation wherever a computer may hold relevant evidence.

Disk imaging and analysis Technique: It enables the fraud investigator to discover evidence of transactions that the fraudster thought were inaccessible or had been destroyed. They can be used where evidence of the commission of a fraud may have been retained in a computer. For example, such evidence may be in the form of word processing documents showing the stages in creation of a forged invoice or a blackmail letter; or files which

demonstrate that an employee has been sending confidential information by e-mail to a competitor or copies of passwords of other members of staff or users of other computers or pornographic material.

The stages are as follows:

- (i) Using specialist hardware and software without the suspect necessarily being alerted, an exact copy of the computer hard disk is taken leaving the original completely intact and leaving no trace of the copying process. This is achieved by attaching the imaging hardware to the parallel port of the computer and running the imaging software without using the computer's operating system. This preserves the integrity of the hard disk and the confidentiality of the investigation. The image is written directly to an optical disk which can then be copied onto a CD ROM for investigative purposes.
 - (ii) The image copy of the disk is processed and areas of storage containing partially overwritten files and files which have been marked as deleted but not overwritten are recovered.
 - (iii) The final stage is the analysis of the processed image. This is done by search software, which can be programmed to find references to suspect transactions. The search is across all the text on the disk so that files which the suspect thinks have been destroyed and data which he may well have had no idea was being retained are searched.
17. (a) The Information Technology Act, 2000 aims to provide the legal framework under which legal sanctity is accorded to all electronic records and other activities carried out by electronic means. The Act states that unless otherwise agreed, an acceptance of contract may be expressed by electronic means of communication and the same shall have legal validity and enforceability.

The objectives of the Act are:

- (a) to grant legal recognition for transactions carried out by means of electronic data interchange and other means of electronic communication commonly referred to as "electronic commerce" in place of paper based methods communication;
 - (b) to give legal recognition to Digital Signature for authentication of any information or matter which requires authentication under any law;
 - (c) to facilitate electronic filing of documents with Government departments.
 - (d) to facilitate electronic storage of data;
 - (e) to facilitate and give legal sanction to electronic fund transfers between banks and financial institutions
 - (f) to give legal recognition for keeping books of account by Bankers in electronic form.
 - (g) to amend the Indian Penal Code, the Indian Evidence Act, 1872, the Bankers' Book Evidence Act, 1891 and the Reserve Bank of India Act, 1934.
- (b) The following chapters are described in the information technology act 2000. They are

Scope of the Act and Definitions [Chapter I]

This Act is called the Information Technology Act, 2000. It shall extend to the whole of India and, unless otherwise provided in the Act, it applies also to any offence or contravention thereunder committed outside India by any person.

Authentication of electronic records using digital signatures [Chapter-II]

This chapter gives legal recognition to electronic records and digital signatures. It contains only section 3. The section provides the conditions subject to which an electronic record may be authenticated by means of affixing digital signature.

Electronic Governance [Chapter III]

It specifies the procedures to be followed for sending and receiving of electronic records and the time and the place of the dispatch and receipt.

Attribution, Receipt and Dispatch of Electronic Records [Chapter IV]

The Act deals with attribution, receipt and dispatch of electronic records. 'Attribution' with regard to a certain means 'to consider it to be written or made by someone.'

Secure Electronic Records And Secure Digital Signatures [Chapter V]

it sets out the conditions that would apply to qualify electronic records and digital signatures as being secure.

Regulation Of Certifying Authorities [Chapter VI]

it contains detailed provisions relating to the appointment and powers of the Controller and Certifying Authorities.

Duties of Certifying Authorities [Section 30]

- (1) This section provides that every Certifying Authority shall follow certain procedures in respect of Digital Signatures as given below:
 - (a) make use of hardware, software, and procedures that are secure from intrusion and misuse;
 - (b) provide a reasonable level of reliability in its services which are reasonably suited to the performance of intended functions
 - (c) adhere to security procedures to ensure that the secrecy and privacy of the digital signatures are assured and
 - (d) observe such other standards as may be specified by regulations.
- (2) Every Certifying Authority shall also ensure that every person employed by him complies with the provisions of the Act, or rules, regulations or orders made thereunder.
- (3) A Certifying Authority must display its licence at a conspicuous place of the premises in which it carries on its business and a Certifying Authority whose licence is suspended or revoked shall immediately surrender the licence to the Controller.

Digital Signature Certification [Chapter VII]

Chapter VII of the Act contains Section 35 to 40

It lays down the procedure for issuance of a Digital Signature Certificate. It provides that an application for such certificate shall be made in the prescribed form and shall be accompanied by a fee not exceeding Rs.25,000.

The section also provides that no Digital Signature Certificate shall be granted unless the Certifying Authority is satisfied.

Duties Of Subscribers [Chapter VIII]

A subscriber shall be deemed to have accepted a Digital Signature Certificate if he publishes or authorises the publication of such signature to one or more persons or otherwise demonstrates his approval of the Digital Signature Certificate.

Penalties And Adjudication [Chapter IX]

It provides for awarding compensation or damages for certain types of computer frauds. It also provides for the appointment of Adjudicating Officer for holding an inquiry in relation to certain computer crimes and for awarding compensation.

Cyber Regulations Appellate Tribunal [Chapter X]

The “Cyber Regulations Appellate Tribunal” has appellate powers in respect of orders passed by any adjudicating officer. Civil courts have been barred from entertaining any suit or proceedings in respect of any matter which an adjudicating officer or Tribunal is empowered to handle.

Offences [Chapter XI]

It deals with some computer crimes and provides for penalties for these offences.

Network Service Providers Not To Be Liable In Certain Cases [Chapter XII]

It contains section 79 which provides that the Network Service Providers shall be liable for any third party information or data made available by him if he proves that the offence, was committed without his knowledge or consent.

Miscellaneous [Chapter XIII]

The Act confers on the Central Government the power to make rules by notifying in the Official Gazette and the Electronic Gazette, in respect of certain matters.

The State Government may by notification in the Official Gazette, make rules to carry out the provisions of this Act.

18. (a) EDP auditing is needed to evaluate the adequacy of automated information systems to meet processing needs, to evaluate the adequacy of internal controls, and to ensure that assets controlled by those systems are adequately safeguarded.

Concurrent audit techniques use embedded audit modules, which are segments of program code that performs audit functions. They also report test results to the auditor and store the evidence collected for the auditor's review. Concurrent audit techniques are time-consuming and difficult to use, but are less so if incorporated when programs are developed.

Auditors commonly use five concurrent audit techniques.

- (i) An integrated test facility (ITF) technique places a small set of fictitious records in the master files. The records might represent a fictitious division, department, or branch office or a customer or supplier. Processing test transactions to update these dummy records will not affect the actual records.
- (ii) The snapshot technique examines the way transactions are processed. Selected transactions are marked with a special code that triggers the snapshot process. Audit modules in the program record these transactions and their master file records before and after processing.
- (iii) SCARF (system control audit review file) uses embedded audit modules to continuously monitor transaction activity and collect data on transactions with special audit significance. The data are recorded in a SCARF file or audit log. Transactions that might be recorded in a SCARF file include those exceeding a specified rupee limit, involving inactive accounts, deviating from company policy, or containing write-downs of asset values.
- (iv) Audit hooks are audit routines that flag suspicious transactions. They devised a system of audit hooks to tag records with a name or address change. The internal audit department is now notified when a tagged record is associated with a withdrawal and can appropriately investigate the transaction for fraud.
- (v) Continuous and intermittent simulation (CIS) embeds an audit module in a data base management system. The CIS module examines all transactions that update the DBMS using criteria similar to those of SCARF. If a transaction has special audit significance, the module independently processes the data (in a manner similar to parallel simulation), records the results, and compares them with those obtained by the DBMS.

- (b) The IS auditor is responsible for establishing control objectives that reduce or eliminate potential exposure to control risks. After the objective of the audit has been established, the auditor must review the audit subject and evaluate the results of the review to determine areas that require correction or improvement.

The purpose of an AIS audit is to review and evaluate the internal controls that protect the system. When performing an IS audit, auditors should ascertain that the following objectives are met:

1. Security provisions protect computer equipment, programs, communications, and data from unauthorized access, modification, or destruction.
 2. Program development and acquisition is performed in accordance with management's general and specific authorization.
 3. Program modifications have the authorization and approval of management.
 4. Processing of transactions, files, reports, and other computer records is accurate and complete.
 5. Source data that is inaccurate or improperly authorized is identified and handled according to prescribed managerial policies.
 6. Computer data files are accurate, complete, and confidential.
19. (a) Information Security help to ensure the smooth functioning of information systems and protect the organization from loss or embarrassment caused by security failures.

Security relates to the protection of valuable assets against loss, disclosure, or damage. Securing valuable assets from threats, sabotage, or natural disaster with physical safeguards such as locks, perimeter fences, and insurance is commonly understood and implemented by most organizations. However, security must be expanded to include logical and other technical safeguards such as user identifiers, passwords, firewalls.

The objective of information security is "the protection of the interests of those relying on information, and the information systems and communications that deliver the information, from harm resulting from failures of availability, confidentiality, and integrity".

The security objective is supported by eight core principles-accountability, awareness, multidisciplinary, cost effectiveness, integration, reassessment, timeliness, and societal factors. Each core principle is briefly discussed below:

1. Accountability: Responsibility and accountability must be explicit.
 2. Awareness: Awareness of risks and security initiatives must be disseminated.
 3. Multidisciplinary: Security must be addressed taking into consideration both technological and non-technological issues.
 4. Cost Effectiveness: Security must be cost-effective.
 5. Integration: Security must be coordinated and integrated.
 6. Reassessment: Security must be reassessed periodically.
 7. Timeliness: Security procedures must provide for monitoring and timely response.
 8. Societal Factors: Ethics must be promoted by respecting the rights and interests of others.
- (b) There are two basic types of protection that an organization can use: Preventative and Restorative.
- (i) Preventative Information Protection: This type of protection is based on use of security controls. Information security controls are generally grouped into three types of control: Physical, Logical, and Administrative. Organizations require all three types of controls. The organization's Information Security Policy through the associated Information Security Standards documentation mandates use of these controls.

- (ii) Restorative Information Protection: Security events that damage information will happen. If an organization cannot recover or recreate critical information in an acceptable time period, the organization will suffer and possibly have to go out of business. Planning and operating an effective and timely information backup and recovery program is vital to an operation. Information backup does not simply involve backing up "just the valuable information," but it frequently also means backing up the system as well. The key requirement of any restorative information protection plan is that the information can be recovered.
 - (iii) Holistic Protection: Protecting corporate information from harm or loss is not an easy task. Protection must be done holistically and give the organization the appropriate level of security at a cost that is acceptable to the business. One must plan for the unexpected and unknown, expect the worst events to happen, and recover from these events if and when they occur, as though nothing ever happened.
20. (a) CASE provides the software engineer with the ability to automate manual activities and to improve engineering insight. like computer-aided engineering and design tools that are used by engineers in other disciplines, case tools help to ensure that quality is designed in before the product is built.

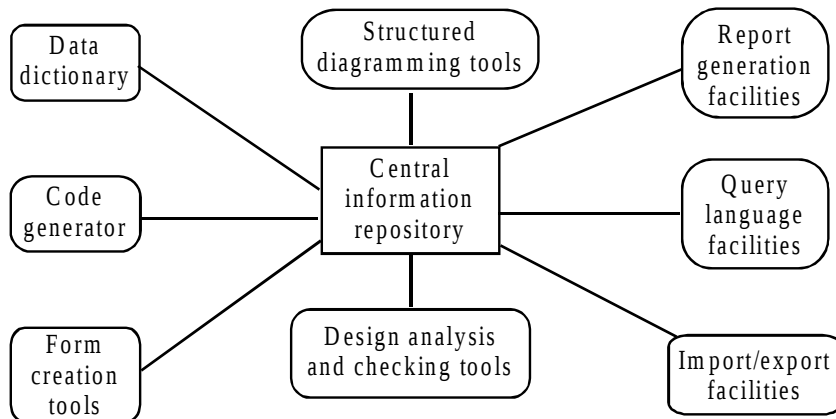
CASE stands for 'Computer Aided Software Engineering'. CASE TOOLS are automated software tools. CASE encompasses computer-based procedures, techniques, and tools, which can be used to develop, maintain and reengineer software. The CASE tools can be used as a single tool or they can be integrated into a common framework of environment such as Integrated Project Support Environment(IPSE) where team of software engineers work together to produce software.

Integrated CASE tools: Specialized CASE tools can be combined together to provide a wider support to software process activities. An effective integration for framework makes evolution possible as new systems are added without disturbing the existing systems. In system engineering environment, there are five different levels of integration of CASE tools which are possible.

1. Platform integration: Tools run on the same hardware/operating system platform.
 2. Data integration: Tools operate using a shared data model.
 3. Presentation integration: Tools offer a common user interface.
 4. Control integration: Tools may activate and control the operation of other tools.
 5. Process integration: Guided by a process model.
- (b) CASE work benches are available to support most software process activities.
- Analysis and design work benches: Analysis and design work benches are designed to support the analysis and design stages of the software process where models of the system are created. The components of this model are
- (a) Diagram editors to create data flow diagrams, structured charts, entity relationship diagram and so on.
 - (b) Design analysis and checking tools which process the design and then submit report on errors and anomalies. These are integrated with editing system so that user errors are trapped at an early stage in the process.
 - (c) Repository query languages which allow the designer to find the designs and associate design information in the repository.
 - (d) A data dictionary which maintains information about the entities used in a system design.
 - (e) Report definition and generation tools which take information from the central store and automatically generate system documentation.

- (f) Forms definition tools which allow screen and document formats to be specified.
- (g) Import-export facilities which allow the interchange of information from the central repository with other development tools .
- (h) Code generators which generate code or code skeletons automatically from the design captured in the central store.

An Analysis and Design work bench



21. (i) **Ratio Analysis:** Ratios provide very useful tools for the manager to assess the organization by making two basic types of comparisons. First, the analyst can compare a present ratio with past (or expected) ratios for the organization to determine if there has been an improvement or deterioration or no change over time. Second, the ratios of one organization may be compared with similar organizations or with industry averages at the same point in time making sure that "apples are compared with apples and oranges with oranges." This is a type of "benchmarking" so that one may determine whether the organization is "average" in performance or doing better or worse than others.

One important benefit of having an up-to-date accounting system with a flexible reporting facility on a powerful computer is the speed with which complex business calculations can be provided with the information necessary to ensure that they are valid. A frequently used outcome of business calculations is the ratio – a comparison between two numerical values obtained by dividing one by the other. A ratio that compares one production period with another can be a useful indicator to guide internal management. The financial position of the company can be compared with that of a rival company by means of one or more ratios. Ratios between individual company performance and consolidated financial statement amounts can be used to explain or amplify the annual report. There are certain financial ratios which help financial personnel make better use of financial information in planning and control.

These ratios can be broadly classified into three main areas. They are

1. Profitability.
 2. Liquidity.
 3. Efficiency or Activity.
- (ii) **Meta-CASE Workbenches:** Meta case work benches are CASE tools which are used to generate other CASE tools. They are usually based on a description of the rules and notations of design or analysis methods. There are five different aspects which are to be considered in Meta-case workbench.
- (a) A data model for data capture and output generation.
 - (b) A frame model which defines the views of the data model to be generated. Each

possible view of the data model is termed as frame. Links between frames which allow navigation from one representation to another are defined in this model.

- (c) Diagrammatic notation for each diagram frame.
 - (d) Textual presentation for each text frame.
 - (e) Report structures.
- (iii) **Digital Signature:** In cryptography, a digital signature or digital signature scheme is a type of asymmetric cryptography used to simulate the security properties of a signature in digital, rather than written, form. Digital signature schemes normally give two algorithms, one for signing which involves the user's secret or private key, and one for verifying signatures which involves the user's public key. The output of the signature process is called the "digital signature."

Digital signatures, like written signatures, are used to provide authentication of the associated input, usually called a "message." Messages may be anything, from electronic mail to a contract, or even a message sent in a more complicated cryptographic protocol. Digital signatures are used to create public key infrastructure (PKI) schemes in which a user's public key (whether for public-key encryption, digital signatures, or any other purpose) is tied to a user by a digital identity certificate issued by a certificate authority. PKI schemes attempt to unbreakably bind user information (name, address, phone number, etc.) to a public key, so that public keys can be used as a form of identification.

For more details of the above points, students are advised to refer to the study material Chapter-16, Section 16.3 and web link , [http://en.wikipedia.org/wiki/digital signature](http://en.wikipedia.org/wiki/digital%20signature)

- (iv) **Check Digits:** A check digit is a control digit (or digits) added to the code when it is originally assigned that allows the integrity of the code to be established during subsequent processing. The check digit can be located anywhere in the code, as a prefix, a suffix, or embedded someplace in the middle. Whenever the code is transcribed from one document to another this check is to be effected. There are numerous other check digit schemes but the 11 – module check digit scheme has been empirically established as the best to detect the transposition errors commonly encountered in data processing situations.
- (v) **Integrated Enterprise Management:** Enterprise can be managed by using an Integrated Enterprise Management. This consists of getting accounting data prepared by subsidiaries for corporate reporting which will be automatically prepared simultaneously within the local books of each subsidiary. This data is transferred to a module called Enterprise Controlling (EC).

It is easy to transfer the data to the EC module to automatically set up consolidated financial statements including elimination of inter-company transactions, currency translation etc.

Enterprise Controlling consists of 3 modules.

1. EC-CS.
2. EC-PCA
3. EC-EIS.

It allows to control the whole enterprise from a corporate and a business unit perspective within one common infrastructure. It helps to speed up provision of business control information by fully automated corporate reporting from operative accounting via financial consolidation to management reporting.

- (vi) **Encryption:** is the process of transforming information (referred to as plaintext) to make it unreadable to anyone except those possessing special knowledge, usually referred to as a key. The result of the process is encrypted information (in cryptography, referred to as ciphertext). Many database systems use encryption procedures to protect highly sensitive data, such as product formulas, personnel pay rates, password files, and certain financial data. Encryption uses an algorithm to scramble selected data, thus making it unreadable to

an intruder “browsing” the database. In addition to protecting stored data, encryption is used for protecting data that are transmitted across networks.

For more details of the above points, students are advised to refer to the study material Chapter-13, Section 13.3 and web link , <http://en.wikipedia.org/wiki/encryption>

- (vii) Client/Server Security: Client / server computing allows applications to be broken down into many different jobs. “Each task can be run on a different platform, under a different operating system with a different network protocol. Each task can be developed and maintained separately, accelerating application development.” Applications can be divided into six different tasks which include user interface, presentation logic, application logic, data requests and results acceptance, data integrity, and physical data management enabling many different IS professionals to work on the same application at the same time.

There are certain security techniques which are used to implement the C/S technology.

- Access to data and application is secured by disabling the floppy disk drive.
- Diskless workstation prevents unauthorized access.
- Unauthorized users may be prevented from overriding login scripts and access by securing automatic boot or startup batch files.
- Network monitoring can be done to know about the client so that it will be helpful for later investigation, if it is monitored properly.
- Data encryption techniques are used to protect data from unauthorized access.
- Authentication systems can be provided to a client, so that they can enter into system, only by entering login name and password.
- Smart cards can be used. It uses intelligent hand held devices and encryption techniques to decipher random codes provided by client-server based operating systems.
- Application controls may be used and users will be limited to access only those functions in the system that are required to perform their duties.

- (viii) Hash Function: means an algorithm mapping or translation of one sequence of bits into another, generally smaller, set known as “hash result” such that an electronic record yields the same hash result every time the algorithm is executed with the same electronic record as its input making it computationally infeasible—

- (a) to derive or reconstruct the original electronic record from the hash result produced by the algorithm;
- (b) that two electronic records can produce the same hash result using the algorithm.

The digital signature is created in two distinct steps. First the electronic record is converted into a message digest by using a mathematical function known as “hash function” which digitally freezes the electronic record thus ensuring the integrity of the content of the intended communication contained in the electronic record. Any tampering with the contents of the electronic record will immediately invalidate the digital signature. Secondly, the identity of the person affixing the digital signature is authenticated through the use of a private key which attaches itself to the message digest and which can be verified by anybody who has the public key corresponding to such private key. This will enable anybody to verify whether the electronic record is retained intact or has been tampered with since it was so fixed with the digital signature. It will also enable a person who has a public key to identify the originator of the message.

- (ix) File Sharing Architecture: The original PC networks were based on file sharing architectures, where the server downloads files from the shared location to the desktop environment. The requested user job is then run in the desktop environment. The traditional file server architecture has many disadvantages especially with the advent of less expensive but more powerful computer hardware. The server directs the data while the workstation

processes the directed data. Essentially this is a dumb server-smart workstation relationship. The server will send the entire file over the network even though the workstation only requires a few records in the file to satisfy the information request.

- (x) **Virus:** A virus is a program (usually destructive) that attaches itself to a legitimate program to penetrate the operating system. The virus destroys application programs, data files, and operating systems in a number of ways. One common technique is for the virus to simply replicate itself over and over within the main memory, thus destroying whatever data or programs are resident. One of the most insidious aspects of a virus is its ability to spread throughout the system and to other systems before perpetrating its destructive acts. Typically, a virus will have a built-in counter that will inhibit its destructive role until the virus has copied itself a specified number of times to other programs and systems. The virus thus grows geometrically, which makes tracing its origin extremely difficult.

Virus programs usually attach themselves to the following types of files:

1. An .EXE or .COM program file
2. The .OVL (overlay) program file
3. The boot sector of a disk
4. A device driver program

When a virus-infected program is executed, the virus searches the system for uninfected programs and copies itself into these programs. The virus in this way thus spreads to the applications of other users or to the operating system itself.

PAPER – 7 : DIRECT TAXES

QUESTIONS

1. Discuss whether the expenditure incurred in connection with issue of shares is allowable as a business expenditure. Will your answer be the same in respect of expenditure incurred on account of stamp duty and registration fees in connection with issue of bonus shares?
2. The scope of disallowance under section 40(a)(ia) in respect of payments to residents without deduction of tax at source has been expanded. Is the statement correct? Elucidate.
3. Discuss the provisions regarding taxability of gifts received on or after 1.4.06.
4. Mr.X was engaged in smuggling business. Foreign currency equivalent to Rs.4,56,980 seized from his custody was the amount involved in the smuggling activity. Mr.X contended that confiscation of foreign currency equivalent to Rs.4,56,980 was a loss of his stock-in-trade and therefore, the same should be allowed as business loss. Discuss the correctness of contention of Mr.X.
5. Mr.Ganesh, who was a civil contractor, filed his return of income for the assessment year 2005-06. The assessment was made but was cancelled under section 263. Thereafter, the Assessing Officer, made a best judgment assessment under section 144 applying the net profit rate on contract receipts to estimate the income from contract work. Further, he made separate addition on account of introduction of unexplained cash and unexplained payments for purchases outside the books of account. Discuss whether the Assessing Officer can make a separate addition on account of unexplained cash and unexplained payments for purchases where he has applied the net profit rate on contract receipts for estimating the income from contract work.
6. Armstrong Ltd., a manufacturing company, which maintains accounts under mercantile system has disclosed a net profit of Rs.25 lakhs for the year ending 31st March, 2007. Compute the taxable income of Armstrong Ltd. for the A.Y. 2007-08, after considering the following information, giving reasons for each adjustment:
 - (i) Advertisement expenditure includes a sum of Rs.1,20,000 paid in cash to the sister concern of a director, the market value of which is Rs.1,04,000.
 - (ii) Legal charges include a sum of Rs.90,000 paid to a consultant for framing a scheme of amalgamation duly approved by the Central Government.
 - (iii) Repairs of plant and machinery includes Rs.3.60 lakhs towards replacement of worn out parts of machineries.
 - (iv) A sum of Rs.12,000 on account of liability foregone by a creditor has been taken to general reserve. The same was charged to the Revenue Account in the Assessment Year 2002-03.
 - (v) Sale proceeds of import entitlements amounting to Rs.2 lakh has been credited to Profit & Loss Account, which the company claims as capital receipt not chargeable to income-tax.
 - (vi) The company is also engaged in the biotechnology business, for which it incurred the following expenditure on in house research and development as approved by the prescribed authority:
 - (a) Research equipments purchased Rs.3,00,000.
 - (b) Remuneration paid to scientists Rs.1,00,000.

The total amount of Rs.4,00,000 has been debited to the Profit & Loss account.
7. Does conversion of unpaid interest into a funded interest term loan tantamount to payment of interest for the purpose of claim of deduction? What is the tax treatment of subsequent repayment of funded interest term loan?
8. What is meant by "Anonymous donation"? Which are the entities in whose hands such receipts are taxable? Discuss the taxability of anonymous donations received by –
 - (a) Wholly charitable trusts/institutions;

- (b) Wholly religious trusts/institutions;
- (c) Partly charitable and partly religious institutions/trusts.

9. Explain the Scheme for submission of returns through Tax Return Preparers.
10. A company filed its return of income for the relevant assessment year without claiming deduction under section 80-IB. Later on, it sought to claim the deduction by way of a letter addressed to the Assessing Officer. The deduction was disallowed by the Assessing Officer on the ground that there was no provision under the Act to make amendment in the return of income by making an application at the assessment stage without revising the return. Discuss the correctness of the contention of the Assessing Officer.
11. The accounts of Beta Ltd., a domestic company prepared in accordance with the provisions of Part II and Part III of Schedule VI to the Companies Act, reveal the following position -

Particulars	Rs.
Profit before depreciation	150 lakhs
Less: Current year depreciation	20 lakhs
Net profit	<u>130 lakhs</u>

The previous year of the company is the financial year ending 31.3.2007.

The profit computed under the head "Profits and gains of business or profession" in accordance with the provisions of the Income-tax Act is as under –

Particulars	Rs.
Profit before depreciation	160 lakhs
Less: Depreciation as per Income-tax Rules	120 lakhs
Balance	<u>40 lakhs</u>

The profit of Rs.160 lakhs includes Rs.20 lakhs qualifying for deduction under section 80-IB.

The company is eligible to carry forward the following amounts from A.Y.2006-07 -

Particulars	Rs.
Unabsorbed depreciation	10 lakhs
Business loss	5 lakhs

It may be assumed that the unabsorbed depreciation and business loss are the same under the Income-tax Act and Companies Act.

You are required to examine –

- (i) the applicability of section 115JB; and
 - (ii) the availability of tax credit in the subsequent years.
12. Discuss the validity of the notice issued under section 142 after the end of the relevant assessment year, with reference to the amendment made by the Finance Act, 2006. Is there any benefit in issuing notice under section 142(1) instead of issuing notice under section 148? Explain.
 13. Discuss the amendments made by the Finance Act, 2006 relating to the following provisions of Minimum Alternate Tax (MAT) –
 - (a) Period of set-off of MAT credit;
 - (b) Rate of MAT and scope of coverage;
 - (c) Manner of computation of book profit.

14. Can the Assessing Officer exercise the power under section 131(3) to impound and retain any documents produced before it in a case of "investigation" or "enquiry" or is it necessary that a "proceeding" should be pending against the specified individual for exercise of such power?
15. The scope of tax deduction at source under section 194-I and 194J has been expanded by the Taxation Laws (Amendment) Act, 2006. Is this statement correct? Elucidate.
16. Are tax deduction provisions under section 194C attracted in respect of supply of corrugated boxes with some labels printed on them? Explain with the aid of a recent case law.
17. The Finance Act, 2006 has alleviated the burden of fringe benefit tax to a certain extent. Discuss, highlighting the areas where such alleviation has been effected.
18. Discuss whether fringe benefit tax liability is attracted in respect of the following expenses -
 - (i) Reimbursement to employees of expenditure incurred by them on food and beverages in the office premises while working after office hours.
 - (ii) Expenditure on group health insurance or group medical insurance.
 - (iii) Per diem allowance given by the employer to employees for meeting the expenditure on lodging and boarding.
 - (iv) Expenditure on capital items like refrigerator, television etc. in a guest house.
 - (v) Rent paid or payable for a financial lease of a motor car.
19. Mr. Paresh had taken a loan of Rs.4 lakh from his relative on the security of his residential house. The outstanding amount of loan as on 31.3.2007 was Rs.3 lakh. The loan was utilized to buy shares and securities. Mr. Paresh claimed the outstanding loan as a deduction while computing his net wealth. Discuss whether such deduction is permissible under the Wealth-tax Act.
20. Sterlite Constructions Ltd. furnishes the following particulars of its wealth for the valuation date 31st March, 2007. Compute its net wealth as on valuation date 31st March 2007.

	Rs.	Rs.
Land in rural area (situated 25 kms away from the municipal limits of Agra)		45,00,000
Land in urban area (for construction of Mall)		40,00,000
Land in urban area (held as stock-in-trade since 1995)		30,00,000
Motor car (including one imported car worth Rs.9 lakhs)		15,00,000
Jewellery (held as stock-in-trade)		12,00,000
Bank balance		7,00,000
Cash in hand as per cash book		3,40,000
Guest house and land appurtenant thereto in rural area		11,00,000
Residential flats of identical size provided to 4 employees for their use near factory in rural areas (salaries of 3 such employees exceed Rs.5,00,000 p.a.)		12,00,000
Residential house provided to managing director (salary exceeds Rs.5,00,000 p.a.)		15,00,000
Flats constructed remaining unsold (not held as stock)		25,00,000
Residential house provided to whole time director (salary Rs.20,000 p.m.)		16,00,000
The company has taken the following loans :		
(a) for purchase of jewellery	8,00,000	
(b) for flats constructed remaining unsold	7,00,000	
(c) for residence provided to whole time director	2,00,000	

SUGGESTED ANSWERS / HINTS

1. The issue as to whether the expenditure in connection with the issue of shares would be allowable as a business expenditure came up recently before the Karnataka High Court in CIT v. Amco Batteries (2006) 155 Taxman 167 (Kar.). The High Court followed the judgment of the Supreme Court in the case of Brooke Bond India Ltd. v. CIT (1997) 225 ITR 798, where it was held that expenditure in connection with issue of shares, with a view to increase its share capital, is directly related to the expansion of the capital base of the company and is a capital expenditure. Hence, expenditure in connection with the issue of shares is not allowable as a business expenditure.

However, the same is not true in respect of expenditure in connection with the issue of bonus shares. The Supreme Court, in CIT v. General Insurance Corporation (2006) 286 ITR 232, observed that there is no inflow of fresh funds or increase in capital employed on account of issue of bonus shares. There is merely a reallocation of company's fund on account of issue of bonus shares by capitalization of reserves. Therefore, the company has not acquired a benefit or advantage of enduring nature. The total funds available with the company will remain the same and there is no change in the capital structure of the company consequent to the bonus issue. Thus, issue of bonus shares does not result in the expansion of capital base of the company. Therefore, the expenditure incurred by the company on account of stamp duty and registration fees for the issue of bonus shares is allowable as revenue expenditure.

2. This statement is correct. So far, as per section 40(a)(ia), failure to deduct tax from interest, commission or brokerage, fees for professional services or fees for technical services payable to a resident or amounts payable to a resident contractor or sub-contractor, or failure to remit such tax after deduction resulted in disallowance of such payments in the computation of income of the payer. This disallowance has now been extended to payments of rent and royalty also with effect from A.Y.2007-08.

Note - The definition of rent has been amended by the Taxation Laws (Amendment) Act, 2006 w.e.f. 13.7.2006. Accordingly, rent means any payment, by whatever name called, under any lease, sub-lease, tenancy or any other agreement or arrangement for the use of (either separately or together) any land or building (including factory building) or land appurtenant to the building (including factory building) or machinery or plant or equipment or furniture or fittings whether or not all or any of the above are owned by the payee. Royalty has the same meaning as given in Explanation 2 to section 9(1)(vi).

3. A new clause (vi) has been inserted in section 56(2) w.e.f. A.Y. 2007-08 to provide that where any sum of money is received without consideration on or after 1.4.2006 by an individual or a Hindu undivided family from any person or persons and the aggregate value of all such sums received during the previous year exceeds Rs.50,000/-, the whole of the aggregate value of such sum shall be included in the total income of such individual or Hindu undivided family under the head "Income from other sources".

However, certain sums of money received have been exempted i.e. any sum of money received -

- (a) from any relative; or
- (b) on the occasion of the marriage of the individual; or
- (c) under a will or by way of inheritance; or
- (d) in contemplation of death of the payer; or
- (e) from any local authority as defined in the Explanation to section 10(20) i.e. Panchayat, Municipality, Cantonment Board or Municipal Committee and District Board, legally entitled to, or entrusted by the Government with, the control or management of a Municipal or local fund; or
- (f) from any fund or foundation or university or other educational institution or hospital or other medical institution or any trust or institution referred to in clause (23C) of section 10; or
- (g) from any trust or institution registered under section 12AA.

4. This issue came up before the Bombay High Court in CIT v. Anil M. Gehi (2006) 284 ITR 338. The assessee was engaged in smuggling business. Foreign currency equivalent to Rs.4,56,980 seized from his custody was the amount involved in the smuggling activity. The High Court observed that confiscation of the amount was, therefore, business loss suffered by the assessee in conducting his business of smuggling. It was not the case of assessee carrying on some other business for which foreign currency was illegally transported out of India. The confiscation of foreign currency equivalent to Rs.4,56,980 was a loss of stock-in-trade of the assessee. When such amount is brought to tax as income of the assessee under section 69A, he is entitled to the benefit of treating the amount confiscated from him as a business loss.

Therefore, in this case, the contention of Mr.X is correct.

5. This issue came up before the Punjab and Haryana High Court in CIT v. Aggarwal Engg. Co. (Jal.) (2006) 156 Taxman 40. In this case, the assessee who was a civil contractor filed his return of income for the relevant assessment year. The assessment was made but was cancelled under section 263. Thereafter, the Assessing Officer, made a best judgment assessment under section 144 applying the net profit rate on contract receipts to estimate the income from contract work. Further, he made separate addition on account of introduction of unexplained cash and unexplained payments for purchases outside the books of account. These additions were deleted by the CIT(A) and Tribunal. The High Court justified the views of the CIT(A) and Tribunal holding that once the net profit rate was applied, no further addition was called for in respect of purchases and introduction of cash.

Therefore, in the case under consideration, the Assessing Officer cannot make a separate addition on account of unexplained cash and unexplained payments for purchases where he has applied the net profit rate on contract receipts for estimating the income from contract work.

6. Computation of taxable income of Armstrong Ltd. for the A.Y. 2007-08

Particulars	Rs.
Net profit as per Profit & Loss account	25,00,000
Add: (a) Items debited to profit and loss A/c but not deductible	
1. Payment of advertisement expenditure of Rs.1,20,000	
(i) Rs.16,000, being the excess payment to a relative disallowed under section 40A(2)	
(ii) As the payment is made in cash and since the remaining amount of Rs.1,04,000 exceeds Rs.20,000, 20% of Rs.1,04,000 (i.e. Rs.20,800) shall be disallowed under section 40A(3)	(+) 36,800
2. Legal charges for framing amalgamation scheme (deductible under section 35DD in five years). 1/5th of Rs.90,000 i.e. Rs.18,000 to be allowed in the current year. Balance Rs.72,000 (Rs.90,000 - Rs.18,000) is to be added back. (See Note below)	(+) 72,000
3. Under section 31, expenditure relatable to current repairs regarding plant, machinery or furniture is allowed as deduction.	
The test to determine whether replacement of parts of machinery amounts to repair or renewal is whether the replacement is one which is in substance replacement of defective parts or replacement of the entire machinery or substantial part of the entire machinery - CIT v. Darbhanga Sugar Co. Ltd. [1956] 29 ITR 21 (Pat).	
Here, the expenditure on repairs does not bring any new asset into existence. Such replacement can only be considered as current repairs. Hence, no adjustment is required.	

Add: Items chargeable as business income but not credited to profit and loss A/c

4. Liability foregone by creditor [taxable under section 41(1)] (+) 12,000

5. Sale proceeds of import entitlements. The sale of the rights gives rise to profits or gains taxable under section 28(iia). As the amount has already been credited to Profit and Loss Account, no further adjustment is necessary.

Less: Amount not debited to profit and loss account but allowable as deduction

6. Expenditure on in house research and development is entitled to a weighted deduction of one and one half times the expenditure so incurred under section 35(2AB)(1)

= 1.5 x 4 lakhs = 6 lakhs

Expenditure of Rs.4,00,000 has already been debited to Profit & Loss Account

Additional deduction of Rs.2 lakh is further allowed (-) 2,00,000

Taxable Income 24,20,800

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

7. Section 43B has been amended by the Finance Act, 2006 inserting therein two clarificatory Explanations, namely, Explanation 3C and Explanation 3D. These Explanations clarify that any sum payable by the assessee as interest on any loan or borrowing or advance shall be allowed as deduction if such interest has been actually paid and any interest which has been converted into a loan or borrowing or advance but has not been actually paid shall not be allowed as deduction in the computation of income. The clarificatory Explanations reiterate the rationale that conversion of interest into a loan or borrowing or advance does not amount to actual payment.

The CBDT has clarified the manner in which the converted interest will be allowed as deduction in its Circular No.7 / 2006 dated 17.7.2006. The unpaid interest, whenever actually paid to the bank or financial institution, will be in the nature of revenue expenditure deserving deduction in the computation of income. Therefore, irrespective of the nomenclature, the deduction will be allowed in the previous year in which the converted interest (i.e. Funded Interest Term Loan) is actually paid.

8. (i) As per the provisions of the Income-tax Act, 1961, tax exemption under section 10(23C) and section 11 are available to certain entities, as briefed in the table below, on fulfillment of the conditions prescribed under the relevant sections -

Entity	Applicable section
Charitable or religious trusts/institutions	11
Universities and other educational institutions	10(23C)(iiiad) and (vi)
Hospitals and other medical institutions	10(23C) (iii ae) and (via)
Notified funds or institutions established for charitable purposes	10(23C)(iv)
Notified trusts or institutions established wholly for public religious purposes or wholly for public religious and charitable purposes	10(23C)(v)

- (ii) Section 115BBC has been inserted to tax anonymous donations received by the above entities at 30%. The balance total income of these entities will be chargeable to tax as per the normal applicable rates.
- (iii) For this purpose, "anonymous donation" means any voluntary contribution referred to in section 2(24)(iia), where the person receiving such contribution does not maintain a record of the identity indicating the name and address of the person making such contribution and such other particulars as may be prescribed.
- (iv) However, the above provision does not apply to a trust or institution created or established wholly for religious purposes.
- (v) Further, anonymous donations to trusts/institutions created or established for partly charitable and partly religious purposes would be taxed only if such anonymous donation are made with a specific direction that such donation is for any university or other educational institution or any hospital or other medical institution run by such trust or institution. Other anonymous donations received by such trusts/institutions are not taxable.

9. Scheme for submission of returns through Tax Return Preparers [Section 139B]

- (i) Section 139B provides that, for the purpose of enabling any specified class or classes of persons to prepare and furnish their returns of income, the CBDT may notify a Scheme to provide that such persons may furnish their returns of income through a Tax Return Preparer authorised to act as such under the Scheme.
- (ii) The Tax Return Preparer shall assist the persons furnishing the return in a manner that will be specified in the Scheme, and shall also affix his signature on such return.
- (iii) A Tax Return Preparer can be an individual, other than -
 - (1) any officer of a scheduled bank with which the assessee maintains a current account or has other regular dealings.
 - (2) any legal practitioner who is entitled to practice in any civil court in India.
 - (3) a chartered accountant.
 - (4) an employee of the 'specified class or classes of persons'.
- (iv) The "specified class or classes of persons" for this purpose means any person other than a company or a person whose accounts are required to be audited under section 44AB (tax audit) or under any other existing law, who is required to furnish a return of income under the Act.
- (v) The Scheme notified under the said section may provide for the following -
 - (1) the manner in which and the period for which the Tax Return Preparers shall be authorised,
 - (2) the educational and other qualifications to be possessed, and the training and other conditions required to be fulfilled, by a person to act as a Tax Return Preparer,
 - (3) the code of conduct for the Tax Return Preparers,
 - (4) the duties and obligations of the Tax Return Preparers,
 - (5) the circumstances under which the authorisation given to a Tax Return Preparer may be withdrawn, and
 - (6) any other relevant matter as may be specified by the Scheme.
- (vi) Every Scheme framed by the CBDT under this section shall be laid before each House of the Parliament while it is in session to make the same effective.
- (vii) If both the houses decide in making any modification of Scheme, then the Scheme will have effect only in such modified form.

(viii) Similarly, if both the Houses decide that any Scheme should not be framed, then such Scheme will thereafter be of no effect.

(ix) However, such modification or annulment should be without prejudice to the validity of anything previously done under that Scheme.

10. This issue was settled by the Apex Court in Goetze (India) Ltd. v. CIT (2006) 284 ITR 323.

In that case, the assessee had relied upon the decision of the Apex court in National Thermal Power Company Ltd. v. CIT (1998) 229 ITR 383, to contend that it was open to the assessee to raise the points of law even before the Appellate Tribunal. In that case, it was held that the Tribunal had jurisdiction to examine a question of law (raised for the first time), which arose from the facts as found by the income-tax authorities and which have a bearing on the tax liability of the assessee.

The Supreme Court held that this decision does not in any way relate to the power of the Assessing Officer to entertain a claim for deduction otherwise than by filing a revised return. Therefore, the assessee can claim deduction only by filing a revised return.

Therefore, in this case, the contention of the Assessing Officer is correct. The company cannot claim deduction under section 80-IB without filing a revised return.

11. In the case of a company, if the income-tax payable on the total income computed under the Income-tax Act for A.Y.2007-08 and subsequent years, is less than 10% of its book profit, such book profit shall be deemed to be the total income of the assessee and the tax payable by the assessee on such total income shall be the amount of income-tax at the rate of 10% plus surcharge plus education cess.

The book profit shall mean the net profit as shown in the profit and loss account prepared in accordance with the provisions of Part II and III of Schedule VI to the Companies Act, 1956 as adjusted by certain specified additions/deductions.

Computation of book profits of Beta Ltd.

Particulars	Rs. in lakh
Net profit as per profit and loss account	130
Less: Business loss b/f (since the same is lower than unabsorbed depreciation)	5
Book profit	<u>125</u>

Computation of total income of Beta Ltd. as per the Income-tax Act

Particulars	Rs. in lakh
Profit before depreciation	160
Less: Depreciation	<u>120</u>
	40
Less: Business loss brought forward	<u>5</u>
	35
Less: Unabsorbed depreciation	<u>10</u>
Gross Total Income	25
Less: Deduction under section 80-IB	<u>20</u>
Total Income	5
Income-tax payable on Rs.5 lakhs @ 30% plus surcharge @10% plus education cess @ 2%	1.683
10% of book profits	12.5

Since the income-tax payable on the total income (i.e. Rs.1.683 lakhs) is less than 10% of book profits (i.e. Rs.12.5 lakhs), such book profit (i.e. Rs.125 lakhs) shall be deemed to be the total income of the assessee and the tax payable by Beta Ltd. on such total income shall be the amount of income-tax at the rate of 10% plus surcharge@10% plus education cess@2%. The effective rate would be 11.22%.

Particulars	Rs.
Book profits deemed as total income as per section 115JB	1,25,00,000
Tax@11.22% on book profits	14,02,500

Eligibility for tax credit in the subsequent years

Section 115JAA provides that where tax is paid in any assessment year in relation to the deemed income under section 115JB(1), the excess of tax so paid over and above the tax payable under the other provisions of the Income-tax Act, will be allowed as tax credit in the subsequent years. The tax credit is, therefore, the difference between the tax paid under section 115JB(1) and the tax payable on the total income computed in accordance with the other provisions of the Act. In this case, it works out to Rs.12,34,200 (i.e. Rs.14,02,500 – Rs.1,68,300). The tax credit shall be allowed to be set off in a year in which tax becomes payable on the total income computed in accordance with provisions of the Act other than section 115JB. This tax credit is allowed to be carried forward for seven assessment years succeeding the assessment year in which the credit became allowable.

12. (i) Section 142(1) provides, inter alia, that for the purposes of making assessment in a case where a person has not filed a return of income within the prescribed time, the Assessing Officer may serve a notice on such person requiring him to furnish the return of income.
- (ii) Section 142(1), even prior to amendment by the Finance Act, 2006, permitted issue of notice after the expiry of time for filing return as prescribed under section 139(1). There was no outer limit for issue of notice.
- (iii) In *Motorola India & Others vs. DCIT 16 TTJ 1*, the special bench of the Appellate Tribunal held that even though no limitation to issue a notice was contained in section 142(1), a period of limitation should be read into it. Accordingly, a notice under section 142(1) could not be issued after the end of the relevant assessment year.
- (iv) In cases where no return of income has been filed within the relevant assessment year, it would be a case of deemed escaped income under Explanation 2 to section 147 and, therefore, notice under section 148 should be issued instead of notice under section 142(1).
- (v) The Finance Act, 2006 has now amended section 142(1) to overrule the decision in *Motorola's* case. It has now been provided that in a case where a person has not made a return of his income within the time allowed under section 139(1) or before the end of the relevant assessment year, the Assessing Officer may serve a notice under section 142(1) requiring such person to furnish his return of income. This is applicable from April 1, 2006. Therefore, such notice can now be issued even after the end of the relevant assessment year.
- (vi) Further, where any notice has been served on or after April 1, 1990 under the aforesaid provision after the end of the relevant assessment year to any person who has not made a return of his income within the time allowed under section 139(1) or before the end of the relevant assessment year, such notice shall be deemed to be a notice served in accordance with the provisions of section 142(1). This provision is applicable retrospectively from April 1, 1990.
- (vii) After this amendment, the department can issue notice either under section 142(1) or under section 148. Notice under section 142(1) saves the department from the requirement of having to record reasons for the belief that income chargeable to tax has escaped assessment.

(viii) It may be noted that the time-limit for completion of assessment under section 153(1) is 21 months from the end of the assessment year in which the income was first assessable. Therefore, since assessment has to be completed within the said period of 21 months, it appears that notice under section 142(1) should also be issued within that period.

13. (i) Period of set-off of MAT credit [Section 115JAA]

- (1) Section 115JAA enables companies to avail credit in respect of MAT paid under section 115JB and carry forward and set-off such credit within a period of 5 assessment years immediately succeeding the assessment year in which the tax credit becomes allowable. If in the subsequent 5 assessment years, a company continues to pay MAT and the credit is not set-off, it shall lapse.
- (2) The period for setting off such tax credit has been increased from 5 years to 7 years w.e.f. A.Y.2007-08.
- (3) For example, if a company pays MAT for the A.Y.2007-08, it will be eligible for tax credit (equal to MAT paid minus the tax payable on the total income computed in accordance with the provisions of the Act), and such tax credit can be carried forward up to and inclusive of A.Y.2014-15 for set-off against the tax payable on the total income.

(ii) Increase in rate of MAT as well as its scope of coverage [Section 115JB]

- (1) Prior to the amendment by the Finance Act, 2006, section 115JB provided that in the case of a company, where 7.5% of its book profit exceeded the tax on its total income, then the book profit shall be deemed to be the total income and the tax payable on such total income shall be 7.5% thereof. Surcharge@10% shall be added to such amount and education cess would be 2% of such income-tax plus surcharge. The effective rate of tax under section 115JB was, therefore, 8.415%.
- (2) The rate of MAT has been increased from 7.5% to 10% of book profits. The effective rate of MAT has, therefore, increased from 8.415% to 11.22%.
- (3) With effect from A.Y.2007-08, if tax on the total income of a company is less than 10% of its book profits, then MAT provisions are attracted and the book profit is deemed to be the total income and tax is payable @ 10% thereof plus surcharge and education cess.
- (4) The effect of this amendment is that more companies would fall under the MAT net, since, those companies whose tax on total income is higher than 7.5% of book profits but lower than 10% of book profits would also be required to pay MAT. Further, their tax burden and cash outflow would be higher on account of the increase in rate of MAT from 7.5% to 10%.
- (5) For example, for a company, say A Ltd., if the tax payable on the total income is Rs.9.5 lakhs and the book profit is Rs.100 lakhs, MAT provisions would not have been attracted under the earlier provisions since tax on total income is higher than Rs.7.5 lakhs (i.e. 7.5% of book profit). However, w.e.f. A.Y.2007-08, MAT provisions would be attracted in this case, since tax on total income (i.e. Rs.9.5 lakhs) is less than Rs.10 lakhs (i.e. 10% of Rs.100 lakhs). Therefore, the book profits of A Ltd. i.e. Rs.100 lakhs shall be deemed to be its total income for A.Y.2007-08 and tax is payable @10% thereof including surcharge and education cess. Hence, the MAT payable by A Ltd. for A.Y.2007-08 would be Rs.11.22 lakhs (10% of Rs.100 lakhs + surcharge @10%+education cess@2%).

(iii) Manner of computation of 'book profit' [Explanation to section 115JB]

Section 115JB prescribes certain adjustments i.e. additions to and deductions from the net profit shown in the profit and loss account prepared in accordance with the provisions of Parts II and III of Schedule VI of the Companies Act, 1956, in order to arrive at the book profit for MAT purposes.

The following changes have been made in the manner of computation of book profit –

- (1) Long-term capital gains on sale of equity shares through a recognized stock exchange on which securities transaction tax (STT) is paid is exempt under section 10(38). One of the adjustments to the book profit is that exempt income under section 10, which is credited to profit and loss account, would be deducted in arriving at the book profit. However, w.e.f. A.Y.2007-08, deduction of such long-term capital gains is not allowed for computing book profit. Consequently, expenditure to earn such income would not be added back to arrive at the book profit. Consequential amendment has been made in section 10(38) to provide that such long term capital gain of a company shall be taken into account in computing the book profit and income-tax payable under section 115JB.
 - (2) In order to check leakage of revenue on account of certain companies resorting to claim of higher depreciation through revaluation of assets, the manner of computation of book profits has been amended to exclude depreciation on account of revaluation of assets while computing book profits. This amendment has been effected in the following manner -
 - (i) First, the net profit as shown in the profit and loss account should be increased by the amount of depreciation debited to the profit and loss account.
 - (ii) Then, the amount of depreciation debited to the profit and loss account (excluding the claim of depreciation on account of revaluation of assets) should be reduced from the net profit, while arriving at the book profit.
 - (3) In order to avoid double taxation on this score, any amount withdrawn from the revaluation reserve and credited to the profit and loss account, to the extent it does not exceed the amount of depreciation on revaluation of assets, shall be reduced for computing book profits.
14. This question came up before the Delhi High Court in *Suman Sehgal v. Union of India* (2006) 154 Taxman 195. The High Court observed that section 131(3) which talks of specific power of impounding is expressly subject to the rules framed under section 131(1) or 131(1A). Section 131(1) makes a specific reference to four situations – discovery, production of evidence, issuing commissions etc. Section 131(1A) makes a specific reference to investigation and enquiry. The subsequent specific power of impounding under section 131(3) is expressly subject to the rules framed under section 131(1) or 131(1A). Therefore, the Parliament intended the power to impound to be adjunct and concomitant to the express powers indicated in sections 131(1) and 131(1A). Hence, there should be no distinction drawn between investigation and proceeding. The High Court also observed that, from another perspective of viewing, even an investigation or enquiry is, in broad terms, a proceeding.
- Therefore, the High Court held that for exercise of power under section 131(3) by the income-tax authorities to impound and retain documents, it is not necessary that a “proceeding” should be pending against a particular or specified individual. Such power can be exercised even in case of investigation and enquiry.
15. This statement is correct. Under section 194-I, tax is required to be deducted at source on payment of rent. The term rent has been defined in the Explanation to the said section to, inter alia, mean payment for the use of any land or building (including factory building) together with furniture, fittings and the land appurtenant thereto, whether or not such building is owned by the payee. This definition of rent has been expanded to include rent of machinery, plant and equipment also for the purposes of deduction of tax at source under section 194-I.
- Under section 194J(1), tax is required to be deducted at source on payment to a resident, of a sum exceeding Rs.20,000, by way of fees for professional services or fees for technical services at the rate of 5% of such sum. Section 194J(1) has been amended to also include within its fold, payment of royalty and non-compete fees referred to in section 28(va).

16. The Delhi High Court has answered this question in CIT v. Dabur India Ltd.(2006) 283 ITR 197.

The issue under consideration is whether the supply of corrugated boxes with some labels printed on them was a contract for sale and therefore outside the purview of section 194C. The High Court held that printing of the labels on corrugated boxes did not require any special skill or involve any confidence or secrecy. In such circumstances, the predominant object underlying the contract was the sale of goods which took the contract outside the purview of section 194C of the Act.

17. The Finance Act, 2006 has alleviated the burden of fringe benefit tax to a certain extent. The areas where such alleviation has been effected are discussed hereunder -

- (i) Under section 115WB(1)(c) read with section 115WC(1)(b), any contribution by the employer to an approved superannuation fund for employees is liable to FBT in full for A.Y.2006-07. With effect from A.Y.2007-08, contributions by an employer to an approved superannuation fund upto Rs.1 lakh per employee would be exempt from levy of FBT. It may be noted that if the employer's contribution is more than Rs.1 lakh per employee in a year, only the contribution in excess of Rs.1 lakh would be subject to FBT.
 - (ii) The value of fringe benefit in respect of "tour and travel (including foreign travel)" would now be 5% instead of 20%. However, it may be noted that this does not apply to conveyance, for which the value of fringe benefit would continue to be 20%. The effect is that, while the value of fringe benefit in respect of outstation tours and foreign tours has been reduced from 20% to 5%, the value of fringe benefit in respect of local conveyance continues to be 20%. This amendment has been effected by omitting the words "tour and travel (including foreign travel)" from clause (F) of section 115WB(2), which would henceforth read as "Conveyance" w.e.f. A.Y.2007-08. A new clause (Q) has been added in this sub-section which reads as "Tour and travel (including foreign travel)" for which the value of fringe benefits has been specified as 5% in the newly inserted clause (e) of section 115WC(1).
 - (iii) The value of fringe benefit in respect of provision of hospitality [Clause (B) of section 115WB(2)] and use of hotel, boarding and lodging facilities [Clause (G) of section 115WB(2)] would now be 5% instead of 20% for employers engaged in the business of carriage of passengers or goods by ship or by aircraft.
 - (iv) Under the proviso to clause (D) of section 115WB, certain expenditure on advertisement have been excluded from "Sales promotion including publicity". Now, expenditure on distribution of free samples of medicines or of medical equipment to doctors has been excluded from "sales promotion including publicity" and consequently, exempt from levy of FBT.
 - (v) Further, expenditure by way of payment to any person of repute for promoting the sale of goods or services of the business of the employer has also been excluded from "sales promotion including publicity" and consequently, exempt from levy of FBT.
 - (vi) As per section 115WB(1)(a), "fringe benefits" means any consideration for employment provided by an employer by way of any privilege, service, facility or amenity, directly or indirectly, to his employees. However, section 115WB(3) clarifies that the privilege, service, facility or amenity does not include perquisites in respect of which tax is paid or payable by the employee. Further, w.e.f. A.Y.2007-08, any benefit or amenity in the nature of free or subsidized transport or any allowance provided by the employer for journeys by the employees from their residence to the place of work or vice versa is also excluded from the ambit of privilege, service, facility or amenity and consequently, exempt from levy of FBT.
18. (i) Reimbursement to employees of expenditure incurred by them on food and beverages in the office premises while working after office hours – Yes, since only expenditure incurred on food or beverages procured by the employer for providing to his employees in an office or factory is exempt from FBT.

- (ii) Expenditure on group health insurance or group medical insurance – Yes, since it is for the purposes of employee welfare. However, if there is a statutory obligation, the same would not be liable to FBT.
- (iii) Per diem allowance given by the employer to employees for meeting the expenditure on lodging and boarding - Yes. However, the employee is not liable to pay income-tax on any surplus accruing to him from such allowance.
- (iv) Expenditure on capital items like refrigerator, television etc. in a guest house – No, since the proximate object of incurring such expenditure is the acquisition of a capital asset. Depreciation on these assets is also not liable to FBT in the absence of any specific charge.
- (v) Rent paid or payable for a financial lease of a motor car – Yes, since it is in the nature of expenditure on running or maintenance of a motor-car.
19. Mr. Paresh has utilized the loan amount for the purchase of shares and securities which are not “assets” as per section 2(ea) of the Wealth-tax Act. As per section 2(m), “net wealth” means the amount by which the aggregate value, computed in accordance with the provisions of the Act, of all the assets, wherever located, belonging to the assessee on the valuation date, including assets required to be included in his net wealth as on that date under this Act, is in excess of the aggregate value of all the debts owed by the assessee on the valuation date which have been incurred in relation to the said assets. Therefore, only debt incurred in relation to an asset [as per section 2(ea)] is deductible. As shares and securities are not assets, the amount of unpaid loan in respect of these cannot be deducted while computing the net wealth of Mr. Paresh.
20. Computation of net wealth of Sterlite Constructions Ltd. on the valuation date 31.3.2007

Particulars	Rs.	Rs.
1. Land in rural area (not an asset)		-
2. Land in urban area (for construction of mall) [It has been assumed that the land has not been held as stock-in-trade]		40,00,000
3. Land in urban area (held for more than 10 years as stock in trade – hence taxable)		30,00,000
4. Motor car (including imported car)		15,00,000
5. Jewellery (held as stock in trade – hence, not taxable)		Nil
6. Bank balance - not an asset under section 2(ea)		Nil
7. Cash in hand as per cash book - not an asset as per section 2(ea)		Nil
8. Guest house in rural area		11,00,000
9. (a) One residential flat given to an employee, whose salary does not exceed Rs.5,00,000 p.a. - exempt		Nil
(b) Residential flats given to three employees, whose salary exceed Rs.5,00,000 p.a. - taxable		9,00,000
10. Residential house given to Managing Director [It is taxable since his salary exceeds Rs.5,00,000 p.a. It is presumed that the Managing Director is in whole-time employment]		15,00,000
11. Unsold flats [Taxable, since not held as stock-in-trade]		25,00,000
12. Residence given to whole time director (not taxable, since salary does not exceed Rs.5,00,000 p.a.)		Nil
Gross Wealth		1,45,00,000
Less: Debts		
1. Loan for purchasing jewellery – Not deductible since jewellery held as stock in trade is exempt from wealth-tax	Nil	

2. Loan for flats constructed remaining unsold	7,00,000	
3. Loan for residential house provided to the whole time director – not deductible as the house is exempt from wealth-tax	Nil	7,00,000
Net Wealth		<u>1,38,00,000</u>

Amendments made by the Taxation Laws (Amendment) Act, 2006 to
the Income-tax Act, 1961

The Taxation Laws (Amendment) Act, 2006 received the assent of the President on 13.7.2006. The CBDT has issued Circular No.1/2007 dated 27.4.2007, which explains the nature and effect of the amendments made by the Taxation Laws (Amendment) Act, 2006.

(1) Tax Recovery Officer to exercise or perform the powers and functions of the Assessing Officer [Section 2(44)]

- (i) Section 2(44) provides that a Tax Recovery Officer means any income-tax officer who may be authorised by the Chief Commissioner or Commissioner, by a general or special order in writing, to exercise the powers of a Tax Recovery Officer.
- (ii) This clause has been amended to enable a Tax Recovery Officer, if he is authorised by the Chief Commissioner or Commissioner, by general or special order in writing, to exercise the powers and functions which are conferred on, or assigned to, an Assessing Officer under the Income-tax Act, 1961 and which may be prescribed.

(Effective from 13.7.2006)

(2) Exemption of income of North-Eastern Development Finance Corporation Limited [Section 10(23BBF)]

- (i) A new clause (23BBF) has been inserted in section 10 to provide for exemption of any income of the North-Eastern Development Finance Corporation Limited, being a company formed and registered under the Companies Act, 1956.
- (ii) The exemption has been phased out beginning with inclusion of 20% of the total income for tax for the assessment year 2006-07, 40% for the assessment year 2007-08, 60% for the assessment year 2008-09, 80% for the assessment year 2009-10 and 100% from the assessment year 2010-11. The exemption under this clause shall be fully phased out in assessment year 2010-11 and no exemption would be available from such assessment year.

(Effective from A.Y.2006-07)

(3) Removal of the requirement of renewal of notification issued under sub-clauses (iv) and (v) of section 10(23C)

- (i) Under section 10(23C), any notification issued by the Central Government in terms of sub-clause (iv) or sub-clause (v) of the said section has, at any one time, effect for such assessment year or years, not exceeding three assessment years, as may be specified in the notification.
- (ii) In order to dispense with the requirement of periodic renewal of notifications and consequent delays, section 10(23C) has been amended to provide that the restriction of limit of effective period of notification to a maximum of three assessment years shall be applicable in respect of notifications issued by the Central Government under sub-clause (iv) or (v) before 13.7.2006, being the date on which Taxation Laws (Amendment) Bill, 2006 received the assent of the President.
- (iii) Therefore, on account of the above amendment, any notification issued by the Central Government under the said sub-clause (iv) or sub-clause (v), on or after 13.07.2006 will be valid until withdrawn and there will be no requirement on the part of the assessee to seek renewal of the same after three years.

Note – Clause (iv) exempts income of a fund or institution established for charitable purposes and notified by the Central Government and clause (v) exempts income of a trust or institution wholly for public religious purposes or wholly for public religious and charitable purposes, which may be notified by the Central Government.

- (4) Time limit for issue of notification under sub-clauses (iv) and (v) or for approval by the prescribed authority under sub-clauses (vi) and (via) of section 10(23C)
 - (i) Under section 10(23C), in respect of application made by a fund or trust or institution etc. for grant of approval or continuation thereof, there is no time limit for issue of notification under sub-clauses (iv) and (v) or for grant of approval under sub-clauses (vi) and (via) or for passing an order rejecting such application. As a result, there is considerable delay in disposing such applications.
 - (ii) In order to expedite disposal of such applications, it has now been provided that where such an application is made on or after 13.7.2006, every notification under sub-clause (iv) or sub-clause (v) shall be issued or approval under sub-clause (vi) or sub-clause (via) shall be granted or an order rejecting the application shall be passed within the period of 12 months from the end of the month in which such application was received.
- (5) Funds/Trusts/Universities/Other educational institutions or hospitals or other medical institutions referred to in sub-clauses (iv),(v),(vi) or (via) of clause (23C) of section 10 to get their accounts audited and furnish audit report
 - (i) At present, there is no requirement on the part of any fund or trust or institution or any university or other educational institution or any hospital or other medical institution referred to in sub-clauses (iv), (v), (vi) or (via) of section 10(23C) to furnish audited accounts along with the return of income.
 - (ii) It has now been provided that if the total income of any entity referred to in sub-clauses (iv), (v), (vi) and (via) of section 10(23C), without giving effect to the provisions of the said sub-clauses, exceeds the basic exemption limit in any previous year, it shall –
 - (1) get its accounts audited in respect of that year by an accountant as defined in the Explanation below sub-section (2) of section 288; and
 - (2) furnish such audit report along with the return of income for the relevant assessment year. The report must be in the prescribed form, duly signed and verified by the accountant, and must contain such particulars as may be prescribed.

(Effective from A.Y.2006-07)

- (6) Accounts of a charitable or religious trust or institution to be audited if their total income exceeds the basic exemption limit [Section 12A(b)]
 - (i) Section 12A(b) provides that for availing exemption under sections 11 and 12, the accounts of the trust or institution for the previous year should have been audited if the total income of the trust or institution as computed under the Income-tax Act, 1961, without giving effect to the provisions of section 11 and section 12, exceeds Rs.50,000 in that previous year. Such audit report should be furnished along with the return of income for the relevant assessment year in the prescribed form.
 - (ii) Rs.50,000 was the erstwhile basic exemption limit. The basic exemption limit of AOPs has been increased to Rs.1,00,000 by the Finance Act, 2005. Therefore, clause (b) of section 12A has been amended to provide for the requirement of getting the accounts audited if in the previous year the total income exceeds the basic exemption limit.

(Effective from A.Y.2006-07)

- (7) Guidelines, manner and conditions on the basis of which approval is to be granted under section 35(1)(ii) and section 35(1)(iii)
 - (i) So far, there have been no guidelines or manner or conditions in relation to grant of approval of the Central Government to a scientific research association, university, college or other

institution. This has caused undue delay in the processing of applications received for approval from such entities. There was, therefore, a need to provide the step-wise procedure to be followed by the applicants, the manner in which their applications would be processed and the conditions subject to which the approval was to be granted to a scientific research association under clause (ii) of section 35(1) and to a university, college or other institution under clause (iii) of section 35(1).

- (ii) These clauses have, therefore, been amended to lay down that the applicant scientific research association, university, college or other institution shall be approved in accordance with the guidelines, in the manner and subject to such conditions as may be prescribed. The guidelines, manner (including application Forms) and conditions have since been prescribed vide notification bearing S.O. 1856 (E) dated 30.10.2006.
- (iii) The deduction under these clauses would be available only if such association, university, college or other institution is for the time being approved in accordance with the guidelines, in the manner and subject to such conditions as may be prescribed.
- (iv) Further, it has been clarified that the deduction to which an assessee (i.e. donor) is entitled on account of payment of any sum to a scientific research association or university or college or other institution, shall not be denied merely on the ground that subsequent to payment of such sum by the assessee, the approval granted to any of the aforesaid entities is withdrawn.
- (v) Also, it has been provided that the time limit restricting the maximum effective period of a notification to 3 assessment years shall be applicable in respect of a notification issued by the Central Government under clause (ii) or clause (iii) before 13.7.2006. Consequently, any notification issued on or after 13.7.2006 shall remain in force until approval granted to such entity is withdrawn.
- (vi) In respect of an application received on or after 13.7.2006, every notification under clause (ii) or clause (iii) shall be issued or an order rejecting the application shall be passed before expiry of 12 months from the end of the month in which the application for approval was received by the Central Government.

(Effective from A.Y.2006-07)

(8) Deduction not to be denied to the donor-assessee on subsequent withdrawal of approval of specified donee entities[Section 35(2AA), 35AC & 35CCA]

- (i) It has been clarified that the deduction to which an assessee is entitled on account of payment of any sum by him to a National Laboratory, University, Indian Institute of Technology or a specified person for the approved programme [referred to in sub-section (2AA) of section 35] shall not be denied to the donor-assessee merely on the ground that after payment of such sum by him, the approval granted to any of the aforesaid donee-entities has been withdrawn.
- (ii) A similar amendment has been made in section 35AC clarifying that the deduction to which an assessee (i.e. the donor) is entitled on account of payment of any sum by him to a public sector company or a local authority or to an association or institution shall not be denied to the assessee merely on the ground that after payment of such sum by him, the approval granted to such association or institution has been withdrawn or the notification notifying the eligible project or scheme referred to in section 35AC has been withdrawn.
- (iii) A parallel amendment has been made in section 35CCA clarifying that the deduction to which an assessee is entitled on account of payment of any sum by him to an association or institution for carrying out the programme of rural development shall not be denied to the assessee merely on the ground that after payment of such sum by him, the approval granted to such programme or, as the case may be, to the association or institution has been withdrawn.

(Effective from A.Y.2006-07)

(9) Disallowance of rent and royalty paid to a resident without deduction of tax at source [Section 40(a)(ia)]

- (i) As per section 40(a)(ia), failure to deduct tax from interest, commission or brokerage, fees for professional services or fees for technical services payable to a resident or amounts payable to a resident contractor or sub-contractor, or failure to remit such tax after deduction results in disallowance of such payments in the computation of income of the payer.
- (ii) This disallowance has now been extended to payments of rent and royalty. The terms rent and royalty have also been defined. Rent has been defined to have the same meaning as in clause (i) to the Explanation to section 194-I. As per the said clause, rent means any payment, by whatever name called, under any lease, sub-lease, tenancy or any other agreement or arrangement for the use of (either separately or together) any land or building (including factory building) or land appurtenant to the building (including factory building) or machinery or plant or equipment or furniture or fittings whether or not all or any of the above are owned by the payee. Royalty has the same meaning as given in Explanation 2 to section 9(1)(vi).

(Effective from A.Y.2007-08)

(10) Disallowance of expenses for which payment above Rs.20,000 has been made otherwise than by account-payee cheque or account-payee bank draft [Section 40A]

- (i) Section 40A(3), provides for disallowance of 20% of the expenditure if payment in a sum exceeding Rs.20,000 is made, against such expenditure, otherwise than by a crossed cheque or crossed bank draft.
- (ii) Since a crossed cheque or crossed bank draft is a negotiable instrument, endorsement of the same has made it difficult to trace the final payee in many cases. This defeats the purpose of section 40A(3).
- (iii) Since an account payee cheque or account payee bank draft cannot be credited to any account other than the account of the payee, section 40A(3) has been amended to require payments over Rs.20,000 to be made by an account payee cheque drawn on a bank or account payee bank draft.
- (iv) Consequential amendment has been made in section 40A(4) to provide that where any payment has been made by an account payee cheque or account payee bank draft to escape disallowance under section 40A(3), then no person shall be allowed to raise a plea in any suit or other proceeding on the ground that the payment was not made in cash or any other manner.

(Effective from 13.7.2006)

(11) Cash gifts received in excess of Rs.50,000 on or after 1.4.2006 to be taxed under section 56(2)(vi)

- (i) Section 56(2)(v) provides that any sum of money exceeding Rs.25,000 received without consideration by an individual or a Hindu undivided family on or after 1.9.2004 from any person, is chargeable to income-tax under the head "Income from other sources".
- (ii) However, in order to avoid hardship in genuine cases, certain sums of money received have been exempted -
 - (a) any sum received from any relative; or
 - (b) any sum received on the occasion of the marriage of the individual; or
 - (c) any sum received under a will or by way of inheritance; or
 - (d) any sum received in contemplation of death of the payer.
- (iii) It is now provided that the above provisions of clause (v) shall be applicable in respect of any sum of money, exceeding the specified amount, received on or after 1.9.2004 but before 1.4.2006.

- (iv) Further, a new clause (vi) has been inserted in section 56(2) w.e.f. A.Y. 2007-08 to provide that where any sum of money is received without consideration on or after 1.4.2006 by an individual or a Hindu undivided family from any person or persons and the aggregate value of all such sums received during the previous year exceeds Rs.50,000/-, the whole of the aggregate value of such sum shall be included in the total income of such individual or Hindu undivided family under the head "Income from other sources".
- (v) However, certain sums of money received have been exempted i.e. any sum of money received -
- from any relative; or
 - on the occasion of the marriage of the individual; or
 - under a will or by way of inheritance; or
 - in contemplation of death of the payer; or
 - from any local authority as defined in the Explanation to section 10(20) i.e. Panchayat, Municipality, Cantonment Board or Municipal Committee and District Board, legally entitled to, or entrusted by the Government with, the control or management of a Municipal or local fund; or
 - from any fund or foundation or university or other educational institution or hospital or other medical institution or any trust or institution referred to in clause (23C) of section 10; or
 - from any trust or institution registered under section 12AA.
- (vi) For the purposes of the new clause (vi), the term relative has been defined in the Explanation thereto to mean the -
- spouse of the individual;
 - brother or sister of the individual;
 - brother or sister of the spouse of the individual;
 - brother or sister of either of the parents of the individual;
 - any lineal ascendant or descendent of the individual;
 - any lineal ascendant or descendent of the spouse of the individual;
 - spouse of the person referred to in clauses (ii) to (vi).
- (12) Deduction not to be denied to the donor-assessee on subsequent withdrawal of approval of the donee- association, university etc. [Section 80GGA]
- (i) Section 80GGA has been amended by inserting an Explanation each after clause (aa) in respect of the entities covered in clause (a) and clause (aa), clause (b) and clause (bb) of sub-section (2).

Clause	Entity covered	Purpose
(a)	University, college or other institution	Scientific research
(aa)	University, college or other institution	Social science and statistical research
(b)	Association or institution	Rural development, training of persons for implementing rural development programme.
(bb)	Public sector company or a local authority or an association or institution approved by the National Committee.	Carrying out eligible project or scheme referred to in section 35AC.

- (ii) These Explanations clarify that the deduction to which an assessee is entitled in respect of any sum paid to a scientific research association, university, college or other institution or to an association or institution for carrying out the programme of rural development, or to a public sector company, or to a local authority or to an association or institution for carrying out the eligible project or scheme referred to in section 35AC, respectively, shall not be denied merely on the ground that subsequent to the payment of such sum by the assessee the approval granted or, as the case may be, the notification has been withdrawn.

(Effective from A.Y.2006-07)

(13) Specified universities, colleges and other institutions compulsorily required to file their return of income [Section 139(4C) & (4D)]

- (i) Clause (e) of section 139(4C) makes it mandatory for every –
 - (a) fund or institution referred to in section 10(23C)(iv) or
 - (b) trust or institution referred to in section 10(23C)(v) or
 - (c) any university or other educational institution referred to in section 10(23C)(vi) or
 - (d) any hospital or other medical institution referred to in section 10(23C)(via)
 to file a return of income for the previous year, if the total income in respect of which such entities are assessable, without giving effect to the provisions of section 10, exceeds the basic exemption limit. Such return of income should be in the prescribed form and verified in the prescribed manner and should contain such other particulars as may be prescribed. All the provisions of the Income-tax Act shall, to the extent relevant, apply as if it were a return required to be furnished under section 139(1).
- (ii) The scope of the aforementioned provisions of clause (e) of section 139(4C) has been expanded to require any university or other educational institution referred to in section 10(23C)(iiiad) and any hospital or other institution referred to in section 10(23C)(iii ae) to furnish their return of income for the previous year, if the total income in respect of which such entities are assessable, without giving effect to the provisions of section 10, exceeds the basic exemption limit.
- (iii) Sub-section (4D) has been inserted in section 139 to require every university, college or other institution referred to in clause (ii) and clause (iii) of section 35(1), which is not required to furnish its return of income or loss under any other provision of section 139, to furnish its return in respect of its income or loss in every previous year. All the provisions of the Income-tax Act, 1961 shall apply to such return as if it were a return under section 139(1).

(Effective from A.Y.2006-07)

(14) Assessing Officer empowered to send a proposal to the Central Government recommending withdrawal of approval of scientific research association, university, college or other institution approved under section 35(1)(ii) and (iii) [Section 143]

- (i) The guidelines, the manner and the conditions in accordance with which an application made by a scientific research association, university, college or other institution shall be approved under clause (ii) or clause (iii) of sub-section (1) of section 35 have been provided by the Taxation Laws (Amendment) Act, 2006. Also, the amendment provides for grant of one time approval, which means the approval is to remain in force unless it is withdrawn.
- (ii) Therefore, the Assessing Officer is now required to satisfy himself as to the activities of the university, college or other institution referred to in clause (ii) or clause (iii) of section 35(1).
- (iii) If the activities are not being carried out in accordance with all or any of the conditions subject to which any of the said entities had been approved, the Assessing Officer may, after giving a reasonable opportunity of showing cause to the concerned entity, send a proposal to the Central Government recommending withdrawal of approval.

- (iv) The Central Government may, by order, withdraw the approval and forward a copy of the order to the concerned university, college or other institution and to the Assessing Officer.

(Effective from A.Y.2006-07)

- (15) Assessing Officer empowered to rectify assessment order to allow deduction under sections 10A, 10B and 10BA in respect of convertible foreign exchange subsequently received or brought into India [Section 155]

- (i) Under section 155(13), the Assessing Officer has power to rectify an assessment order to allow deduction under sections 80HHB, 80HHC, 80HHD, 80HHE, 80R, 80-O etc. (which was earlier denied on the ground that such income had not been received in convertible foreign exchange in India), when such income is subsequently received or brought into India with the approval of the competent authority.
- (ii) Similar provisions are not available in respect of the provisions of sections 10A, 10B and 10BA, which also provide that foreign exchange may be brought into India within six months from the end of the financial year or within such time as may be extended by the competent authority.
- (iii) Therefore, sub-section (11A) has been inserted in section 155 to provide that where in the assessment for any year, the deduction under section 10A or section 10B or section 10BA has not been allowed on the ground that such income -

- (1) has not been received in convertible foreign exchange in India, or
- (2) having been received in convertible foreign exchange outside India, or having been converted into convertible foreign exchange outside India, has not been brought into India, by or on behalf of the assessee with the approval of the Reserve Bank of India or such other approved authority and

subsequently such income or part thereof has been or is received in, or brought into, India in the manner aforesaid, the Assessing Officer shall amend the order of assessment so as to allow deduction under section 10A or section 10B or section 10BA, as the case may be, in respect of such income or part thereof as is so received in, or brought into, India.

- (iv) The provisions of section 154 shall, to the extent relevant, apply thereto, and the period of four years for making such rectification shall be reckoned from the end of the previous year in which such income is so received in, or brought into, India.

(Effective from 13.7.2006)

- (16) The scope of tax deduction at source on rent under section 194-I expanded

- (i) Under section 194-I, tax is required to be deducted at source on payment of rent.
- (ii) The term rent has been defined in the Explanation to the said section to, inter alia, mean payment for the use of any land or building (including factory building) together with furniture, fittings and the land appurtenant thereto, whether or not such building is owned by the payee.
- (iii) This definition of rent has been amended to provide that the provisions of the said section are applicable whether the items are rented separately or together. Rent of machinery, plant and equipment are also included for the purposes of deduction of tax at source under section 194-I.

(Effective from 13.7.2006)

- (17) Expansion of the scope of tax deduction at source on fees for professional or technical services under section 194J

- (i) Under section 194J(1), tax is required to be deducted at source on payment to a resident, of a sum exceeding Rs.20,000, by way of fees for professional services or fees for technical services at the rate of 5% of such sum.

- (ii) Section 194J(1) has been amended to include within its fold, payment of royalty and non-compete fees referred to in section 28(va). The term royalty has been defined in the Explanation to the amended section and shall have same meaning as in Explanation 2 to section 9(1)(vi).
- (iii) The threshold limit for deduction of tax in respect of each of these payments is Rs.20,000.
(Effective from 13.7.2006)

(18) Time limit for passing penalty order [New sub-section (1A) of section 275]

- (i) Section 275(1) provides the time limit for imposing penalty under Chapter XXI of the Income-tax Act, 1961, as under -
 - (1) In a case where the relevant assessment or other order is the subject matter of an appeal to the Commissioner (Appeals) under section 246 or section 246A or an appeal to the Appellate Tribunal under section 253, an order imposing a penalty shall not be passed –
 - (a) after the expiry of the financial year in which the proceedings, in the course of which action for the imposition of penalty has been initiated, are completed; or
 - (b) six months from the end of the month in which the order of the Commissioner (Appeals) or, as the case may be, the Appellate Tribunal is received by the Chief Commissioner or Commissioner,
 whichever period expires later.
 - (2) However, this limitation is applicable only if the Commissioner (Appeals) passed the order before 1st June, 2003 disposing of the appeal made to him.
 - (3) In a case where the relevant assessment or other order is the subject matter of an appeal to the Commissioner (Appeals) under section 246 or section 246A, and the Commissioner (Appeals) passes the order on or after 1st June, 2003 disposing of such appeal, an order imposing penalty shall be passed –
 - (a) before the expiry of the financial year in which the proceedings, in the course of which action for imposition of penalty has been initiated, are completed; or
 - (b) within one year from the end of the financial year in which the order of the Commissioner (Appeals) is received by the Chief Commissioner or Commissioner,
 whichever is later.
 - (4) In a case where the relevant assessment or other order is the subject matter of revision under section 263 or section 264, an order imposing penalty shall not be passed after the expiry of six months from the end of the month in which such order of revision is passed;
 - (5) In any other case, an order imposing penalty shall not be passed after the expiry of the financial year in which the proceedings, in the course of which action for the imposition of penalty has been initiated, are completed, or six months from the end of the month in which action for imposition of penalty is initiated, whichever period expires later.
- (ii) A new sub-section (1A) has been inserted in section 275 to facilitate the revision of an order for the imposition of penalty or dropping the proceedings for the imposition of penalty, on the basis of subsequent revision of assessment by Commissioner (Appeals) or Appellate Tribunal or High Court or Supreme Court or by the Commissioner under section 263 or section 264.
- (iii) It has been provided that in a case where the relevant assessment or other order is the subject-matter of -
 - (1) an appeal to the Commissioner(Appeals) under section 246 or section 246A; or
 - (2) an appeal to the Appellate Tribunal under section 253; or

- (3) an appeal to the High Court under section 260A; or
- (4) an appeal to the Supreme Court under section 261; or
- (5) revision under section 263 or section 264

and an order imposing or enhancing or reducing penalty or dropping the proceedings for the imposition of penalty is passed before the order of –

- (1) the Commissioner(Appeals); or
- (2) the Appellate Tribunal; or
- (3) the High Court; or
- (4) the Supreme Court

is received by the Chief Commissioner or the Commissioner, or the order of revision under section 263 or 264 is passed, an order imposing or enhancing or reducing penalty or dropping the proceedings for the imposition of penalty may be passed on the basis of assessment as revised by giving effect to such order of the Commissioner(Appeals) or, the Appellate Tribunal or, the High Court, or the Supreme Court or order of revision under section 263 or 264. A revision order under this sub-section can again be revised under this sub-section.

- (iv) It has also been provided that no such order imposing or enhancing or reducing or canceling penalty or dropping the proceedings shall be passed without hearing the assessee or giving him a reasonable opportunity of being heard.
- (v) Further, no such order can be passed after the expiry of six months from the end of the month in which -
 - (1) the order of the Commissioner (Appeals) or the Appellate Tribunal or the High Court or the Supreme Court is received by the Chief Commissioner or the Commissioner; or
 - (2) the order of revision under section 263 or section 264 is passed.
- (vi) Also, it has been provided that the provisions of section 274(2) shall apply in respect of such order imposing or enhancing or reducing penalty.

Note - Section 274(2) provides that for passing an order imposing penalty exceeding Rs.10,000, the Income-tax authority has to take the prior approval of the Joint Commissioner. Also, for passing an order imposing penalty exceeding Rs.20,000, the Assistant Commissioner or the Deputy Commissioner should take the prior approval of the Joint Commissioner.

- (vii) Consequently, section 246A(1) has been amended to provide for an appeal to the Commissioner (Appeals) against an order imposing or enhancing penalty u/s 275(1A).

(Effective from 13.7.2006)

(19) Rounding off of tax payable and refund due [New section 288B]

- (i) Section 288B provides that the amount of tax (including TDS and advance tax), interest, penalty, fine or any other sum payable, and the amount of refund due, under the provisions of the Income-tax Act, shall be rounded off to the nearest rupee.
- (ii) This section has been substituted by a new section to provide that any amount payable, and the amount of refund due, under the provisions of the Income-tax Act, 1961, shall be rounded off to the nearest multiple of ten rupees.
- (iii) For this purpose, any part of a rupee consisting of paise shall be ignored.
- (iv) Thereafter, if such amount is not a multiple of ten, then, if the last figure in that amount is five or more, the amount shall be increased to the next higher amount which is a multiple of ten and if the last figure is less than five, the amount shall be reduced to the next lower amount which is a multiple of ten.

(Effective from 13.7.2006)

IMPORTANT NOTIFICATIONS / CIRCULARS ISSUED BETWEEN 1.5.06 and 30.4.07

I NOTIFICATIONS

(1) Notification No.270/2006 dated 19.9.2006 – Cost Inflation Index for F.Y.2006-07

The Central Government has, vide notification no.270/2006 dated 19.9.2006 specified the cost inflation index for the financial year 2006-07. The CII for F.Y. 2006-07 is 519.

S. No.	Financial Year	Cost Inflation Index
1.	1981-82	100
2.	1982-83	109
3.	1983-84	116
4.	1984-85	125
5.	1985-86	133
6.	1986-87	140
7.	1987-88	150
8.	1988-89	161
9.	1989-90	172
10.	1990-91	182
11.	1991-92	199
12.	1992-93	223
13.	1993-94	244
14.	1994-95	259
15.	1995-96	281
16.	1996-97	305
17.	1997-98	331
18.	1998-99	351
19.	1999-2000	389
20.	2000-01	406
21.	2001-02	426
22.	2002-03	447
23.	2003-04	463
24.	2004-05	480
25.	2005-06	497
26.	2006-07	519

[Notification no.270/2006 dated 19.9.2006]

(2) Notification No.127/2006 dated 1.6.2006 – Notified plan for deduction in respect of annuity plan of LIC

Notification No.	Date	In exercise of powers conferred by	Details
127/2006	1.6.2006	Section 80C(2)(xii)	Jeevan Akshay-III Plan of the LIC of India, as filed by the LIC with the IRDA, as the annuity plan of the LIC for the purposes of section 80C(2)(xii)

- (3) Notification Nos. 142 & 143/2006 dated 29.6.2006 – Notified Bonds for the purpose of exemption of capital gains under section 54EC

The Central Government has notified bonds of National Highways Authority of India (NHAI) and Rural Electrification Corporation Limited (RECL), to be issued during the financial year 2006-07, redeemable after three years, as "long-term specified asset" for the purpose of exemption under section 54EC i.e. capital gains would be exempt to the extent of investment in these notified bonds.

The CBDT has, vide Order F.No.142/09/2006-TPL, dated 30.6.2006, extended the limitation period of six months for making investment under section 54EC of capital gains arising from the transfer of a long-term capital asset to –

- (i) 30.9.2006, in case of persons where the long-term capital asset was transferred between 29.9.2005 and 31.12.2005;
- (ii) 31.12.2006, in case of persons where the long-term capital asset was transferred between 1.1.2006 and 30.6.2006.

- (4) Notification No 380/2006, dated 22.12.2006 – Restriction of maximum investment to Rs.50 lakhs for the purpose of section 54EC

The Central Government has, vide this notification, notified the bonds for an amount of Rs.3,500 crores (redeemable after three years), to be issued by the Rural Electrification Corporation Limited (RECL) during the period between 26.12.2006 to 31.3.2007, as 'long-term specified asset' for the purposes of section 54EC subject to the following conditions, namely:-

- (i) a person who has made an investment of an amount aggregating more than Rs.50 lakh in the bonds of NHAI or RECL notified as long-term specified asset by the Central Government in the Official Gazette for the purposes of section 54EC vide notifications dated 29.6.2006, shall not be allotted any bonds notified as long-term specified asset by this notification;
- (ii) a person who is not covered by clause (i) above, shall not be allotted the bonds notified as long-term specified asset by this notification, for any amount which exceeds the amount of Rs.50 lakh as reduced by the aggregate of the investment, if any, made by him in the bonds of NHAI and RECL notified as long-term specified asset by the Central Government for the purposes of section 54EC of vide notifications dated 29.6.2006.

For example, if one Mr.X has been allotted bonds of NHAI or RECL (vide the above-referred notifications dated 29.6.2006), aggregating to say Rs.52 lakh, he shall not be allotted any further bonds by this notification. If one Mr.Y has been allotted bonds of NHAI or RECL (vide the above-referred notifications dated 29.6.2006) to the extent of say, Rs.30 lakhs, then the allotment of bonds of RECL vide this notification cannot exceed Rs.20 lakhs.

- (5) Notification No.187/2006 dated 20.7.2006 – Conditions to be fulfilled by a public facility to be eligible to be notified as an infrastructure facility in accordance with the provisions of clause (d) of the Explanation to section 36(1)(viii)

Rule 6ABAA has been inserted in the Income-tax Rules, 1962 which specifies the conditions to be fulfilled by a public facility to be eligible to be notified as an infrastructure facility in accordance with the provisions of clause (d) of the Explanation to clause (viii) of sub-section (1) of section 36. The conditions specified therein are -

- (a) it is owned by a company registered in India or by a consortium of such companies or by an authority or a board or a corporation or any other body established or constituted under any Central or State Act;
- (b) it has entered into an agreement with the Central Government or a State Government or a local authority or any other statutory body for (i) developing or (ii) operating and maintaining or (iii) developing, operating and maintaining a new infrastructure facility similar in nature to an infrastructure facility referred to in the Explanation to section 80-IA(4)(i);
- (c) it has started or starts operating and maintaining such infrastructure facility on or after 1st April, 1995.

- (6) Notification No. 188/2006, dated 20.7.2006 – Notification of public facilities as infrastructure facility for the purpose of section 36(1)(viii)

The following public facilities have been notified by the CBDT as infrastructure facility for purposes of section 36(1)(viii)-

- (1) Inland Container Depot and Container Freight Station notified under the Customs Act, 1962
- (2) Mass Rapid Transit system
- (3) Light Rail Transit system
- (4) Expressways
- (5) Intra-urban or semi-urban roads like ring roads or urban by-passes or flyovers
- (6) Bus and truck terminals
- (7) Subways
- (8) Road dividers
- (9) Bulk Handling Terminals which are developed or maintained or operated for development of rail system
- (10) Multilevel Computerised Car Parking.

- (7) Notification No. 267/2006 dated 14.9.2006 – Notification of approved investment under section 11(5)

A new clause (v) has been inserted in rule 17C of the Income-tax Rules, 1962 so as to include as an approved investment under section 11(5), investment by a recognized Stock Exchange, in the equity shares of a company promoted by it to acquire the membership rights of other stock exchanges, where at least 51% of the paid-up share capital is held by the Stock Exchange and the balance is held by its members. The amendment is made effective retrospectively from 26th November, 1999.

- (8) Notification No.314/2006, dated 9.11.2006 – Rule 6DD to provide the cases and circumstances in which payment in a sum exceeding Rs.20,000 may be made otherwise than by an account payee cheque drawn on a bank or by account payee bank draft

Section 40A(3), provides for disallowance of 20% of the expenditure if payment in a sum exceeding Rs.20,000 is made, against such expenditure, otherwise than by a crossed cheque or crossed bank draft. The Taxation Laws (Amendment) Act, 2006 has amended section 40A(3) to require payments over Rs.20,000 to be made by an account payee cheque drawn on a bank or account payee bank draft.

Accordingly, the CBDT has amended Rule 6DD to replace the words “a crossed cheque” and “a crossed bank draft” with “an account payee cheque” and “account payee bank draft” respectively in the heading and content. Therefore, Rule 6DD would henceforth provide the cases and circumstances in which payment in a sum exceeding Rs.20,000 may be made otherwise than by an account payee cheque drawn on a bank or by account payee bank draft.

- (9) Notification No. 357/2006, dated 24.11.2006 - Restriction regarding effective period of approval for the purposes of section 10(23C)(vi) and (via) removed

The CBDT has, vide this notification, amended Rule 2CA, which provides the guidelines for approval under sub-clauses (vi) and (via) of section 10(23C). Sub-rule (3) of Rule 2CA, which restricts the effective period of approval of such university or other educational institution or hospital or other medical institution [covered under sub-clauses (vi)/(via)] by the CBDT or Chief Commissioner or Director General to a maximum of three assessment years, has now been amended to provide that such restrictions would apply only in respect of approvals granted before 1.12.2006.

(10) Notification No. 358/2006, dated 28.11.2006 – Tax Return Preparer Scheme, 2006

The CBDT has, in exercise of the powers conferred by section 139B(1) of the Income-tax Act, 1961, framed the Tax Return Preparer Scheme, 2006, which came into force from 1.12.2006.

As per this scheme, Tax Return Preparer means any individual who has been issued a Tax Return Preparer Certificate and a unique identification number by the Partner Organisation to carry on the profession of preparing the returns of income in accordance with the provisions of this Scheme. However, the following persons are not eligible to act as a Tax Return Preparer -

- (i) any person referred to in clause (ii) or clause (iii) or clause (iv) of sub-section (2) of section 288, namely, any officer of a Scheduled Bank with which the assessee maintains a current account or has other regular dealings, any legal practitioner who is entitled to practice in any civil court in India and an accountant.
- (ii) any person who is in employment and income from which is chargeable to income-tax under the head salaries

Educational qualification for Tax Return Preparers

Any individual who holds a graduation degree from a recognized Indian University in the fields of Business Administration or Management or Commerce or Economics or Law or Mathematics or Statistics shall be eligible to act as Tax Return Preparer.

(11) Notifications 369-374/2006 dated 15.12.2006 – Notification of Zero Coupon Bonds

Section 2(48) defining zero coupon bonds requires that such bonds should be notified by the Central Government. Accordingly, the Central Government has, vide Notifications 369-374 dated 15.12.2006, specified the following bonds to be issued on or before 31.3.2009 by HUDCO, SIDBI, NABARD and IDFC as zero coupon bonds –

- (i) 10 year zero coupon bonds of HUDCO, SIDBI, NABARD and IDFC
- (ii) 15 year zero coupon bonds of HUDCO.

(12) Notification No.1/2007 dated 4.1.2007 – Exemption of interest on tax free municipal bonds issued by Nagpur Municipal Corporation

Section 10(15)(vii) exempts interest on bonds issued by a local authority, if such bonds are specified by the Central Government by notification in the Official Gazette. Accordingly, the Central Government has, vide this notification, specified Tax Free Municipal Bonds issued by Nagpur Municipal Corporation during the F.Y.2006-07, interest from which would be exempt under section 10(15)(vii). However, such benefit would be admissible only if the holder of such bonds registers his or her name and the holding with the Nagpur Municipal Corporation.

(13) Notification No.2/2007 dated 11.1.2007 – Subscription to public deposit scheme of HUDCO to qualify for deduction under section 80C

Deduction under section 80C is available, inter-alia, in respect of any sum paid or deposited in the previous year by the assessee as subscription to any such deposit scheme of a public sector company which is engaged in providing long-term finance for construction or purchase of houses in India for residential purposes, as the Central Government may, by notification in the Official Gazette, specify in this behalf. This has been provided in clause (xvi)(a) of section 80C(2). Accordingly, the Central Government has, vide this notification, specified the Public Deposit Scheme of Housing and Urban Development Corporation Ltd., subscription to which would qualify for deduction under section 80C.

(14) Notification No. 61/2007, dated 28.2.2007 – Investment by way of acquiring equity shares of an incubatee by an incubator to qualify as an approved investment under section 11(5)

Section 11(5) of the Income-tax Act, 1961 specifies the permitted modes of investment by a charitable trust or institution for claiming exemption under section 11. Clause (xii) of section 11(5) specifies that investment can be made by any other mode as may be prescribed. Rule 17C of the Income-tax Rules specifies such other modes of investment. The CBDT has, through the Income-tax (Second Amendment) Rules, 2007, which came into force on 1.3.2007, inserted new clause

(vi) in Rule 17C. Clause (vi) specifies another mode of investment, namely, investment by way of acquiring equity shares of an incubatee by an incubator. Incubatee shall mean such incubatee as may be notified by the Government of India in the Ministry of Science and Technology and incubator shall mean such Technology Business Incubator or Science and Technology Entrepreneurship Park as may be notified by the Government of India in the Ministry of Science and Technology.

(15) Notification No. 67/2007, dated 8.3.2007 – Exemption of interest on Tax Free Municipal Bonds issued by Ahmedabad Municipal Corporation

Sub-clause (vii) of section 10(15) exempts interest on bonds issued by a local authority, if such bonds are specified by the Central Government by notification in the Official Gazette. Accordingly, the Central Government has, vide this notification, specified Tax Free Municipal Bonds issued by Ahmedabad Municipal Corporation during the financial year 2006-07, interest from which would be exempt under section 10(15)(vii). However, this benefit shall be admissible only if the holder of such bonds registers his or her name and the holding with the said Corporation.

II CIRCULARS

(1) Circular No.7/2006 dated 17.7.2006 - Clarification regarding deduction of interest under section 43B in view of clarificatory amendments to section 43B through the Finance Act, 2006

Section 43B was amended by the Finance Act, 2006 inserting therein two clarificatory Explanations, namely, Explanation 3C and Explanation 3D. Both the Explanations clarify that any sum payable by the assessee as interest on any loan or borrowing or advance shall be allowed as deduction if such interest has been actually paid and any interest which has been converted into a loan or borrowing or advance but has not been actually paid shall not be allowed as deduction in the computation of income. The clarificatory explanations only reiterate the rationale that conversion of interest into a loan or borrowing or advance does not amount to actual payment.

The manner in which the converted interest will be allowed as deduction has been clarified in this circular. The unpaid interest, whenever actually paid to the bank or financial institution, will be in the nature of revenue expenditure deserving deduction in the computation of income. Therefore, irrespective of the nomenclature, the deduction will be allowed in the previous year in which the converted interest is actually paid.

(2) Circular No. 8/2006, dated 6.10.2006 - Clarification regarding the meaning of the expression “the produce of animal husbandry” used in sub-clause (ii) of clause (f) of rule 6DD of the Income-tax Rules, 1962

The CBDT had, vide Circular No. 4/2006, dated 29th March, 2006 on the above subject, clarified that the expression “the produce of animal husbandry” used under rule 6DD(f)(ii) would include livestock and meat and in a case where payment exceeding rupees twenty thousand is made to a producer of the products of animal husbandry (including livestock, meat, hides and skins) otherwise than by a crossed cheque drawn on a bank or by a crossed bank draft for the purchase of such produce, no disallowance would be attracted under section 40A(3) read with rule 6DD. It was further clarified that the above exception will not be available in respect of payment for the purchase of livestock, meat, hides and skins from a person who is not proved to be the producer of these goods and is only a trader, broker or any other middleman by whatever name called.

This circular (Circular No.8/2006) gives a clarification as to -

- (i) who are the producers of livestock and meat and
- (ii) the evidence required to be furnished in this regard by the persons making the payments.

The CBDT is of the view that any person, by whatever name called, who buys animals from the farmers, slaughters them and then sells the raw meat carcasses to the meat processing factories or to the traders/retail outlets would be considered as a producer of livestock and meat.

The benefit of rule 6DD of the Income-tax Rules, 1952 shall be available to the person referred to in the above para subject to furnishing of the following :

- (i) A declaration from the person receiving the payment that he is a producer of meat;
- (ii) A confirmation that the payment, otherwise than by an account payee cheque or account payee bank draft, was made on his insistence; and
- (iii) A further confirmation from a veterinary doctor certifying that the person specified in the certificate is a producer of meat and that slaughtering was done under his supervision.

- (3) Circular No.10/2006 dated 16.10.06 - Clarification regarding filing of return of income by the coffee growers being individuals covered by Rule 7B of the Income tax Rules, 1962

The CBDT, vide Circular No. 10/2003 dated 24th December, 2003, had provided that an individual deriving income from growing and curing of coffee, who is not covered by the first proviso to section 139(1), would not be required to file a return of his income if his income from growing and curing of coffee was Rs. 2 lakhs or less. The Finance Act, 2005 has subsequently raised the exemption limit for individual taxpayers from Rs. 50,000 to Rs.1 lakh from the Assessment year 2006-07. The exemption limit in the case of an individual, being a woman resident in India and below the age of 65 years, has been increased to Rs. 1,35,000. In the case of an individual, being a resident in India, who is of the age of 65 or more at any time during the previous year, the exemption limit has been raised to Rs.1,85,000. Therefore, the CBDT has reconsidered the matter of filing of return by the individual coffee growers in order to provide further relief to them and it is clarified that:

- (i) An individual deriving income from growing and curing of coffee would not be required to file his return, if the aggregate of 25% of his income from growing and curing of coffee and income under all other sources liable to tax in accordance with the provisions of this Act, is equal to or less than the exemption limit (1st slab of the rates of Income-tax) prescribed for individual tax payers in the First Schedule of the Finance Act of the relevant year.
- (ii) An individual deriving income from growing, curing, roasting and grounding of coffee with or without mixing chicory or other flavouring ingredients, would not be required to file the return of income if the aggregate of 40% of his income from growing, curing, roasting and grounding of coffee with or without mixing chicory or other flavouring ingredients and income under all other sources liable to tax in accordance with the provisions of this Act, is equal to or less than the exemption limit (1st slab of rates of Income tax) prescribed in the First Schedule of the Finance Act of the relevant year.

- (4) Circular No.13/2006, dated 13.12.2006 - Applicability of TDS provisions of section 194C on contract for fabrication of article or thing as per specifications given by the assessee

The CBDT has clarified the issue regarding the applicability of TDS provisions of section 194C on contract for fabrication of article or thing as per specifications given by the assessee. The CBDT observed that before taking a decision on the applicability of TDS under section 194C on a contract, it would have to be examined whether the contract in question is a contract for work or a contract for sale.

The CBDT clarified that the provisions of section 194C would apply in respect of a contract for supply of any article or thing as per prescribed specifications only if it is a contract for work and not a contract for sale as per the principles in this regard laid down in para 7(vi) of Circular No. 681, dated 8-3-1994. Para 7(vi) of Circular No.681 clarifies that where the property in the article or thing so fabricated passes from the fabricator-contractor to the assessee only after such article or thing is delivered to the assessee, such contract would be a contract of sale and would, therefore, fall outside the purview of section 194C.

PAPER – 8 : INDIRECT TAXES

QUESTIONS

1. With reference to the Central Excise Act, 1944, briefly explain the following:
 - (a) Adjudicating Authority
 - (b) Wholesale dealer
2. Discuss the provisions of the Central Excise Act, 1944 relating to publication of names of persons in certain cases.
3. 'A' manufactures "Pulsator". It received item "Bush" from M/s. Electrolux Voltas Limited. While determining assessable value of the product "Pulsator", 'A' did not include value of "Bush". A show-cause notice is issued to 'A' by the Assistant Commissioner of Excise demanding duty of Rs.75,000 and equivalent amount of penalty under section 11AC of the Central Excise Act, 1944. The Tribunal confirmed the demand. However, it reduced the penalty to Rs.10,000 on the ground that what is laid down in section 11AC is only the maximum amount of penalty and not the minimum.

Do you think the CESTAT is right in reducing the amount of penalty leviable under section 11AC of the Central Excise Act, 1944 without reducing the duty amount? Discuss.
4. Discuss the provisions relating to valuation in case of job-work as provided under rule 10A of the Central Excise Valuation (Determination of Price of Excisable Goods) Rules, 2000.
5. The Commissioner (Appeals) or the Appellate Tribunal may dispense with the pre-deposit demanded under section 35F of the Central Excise Act, 1944 if such deposit would cause undue hardship to the assessee. Discuss with respect to recent decided case laws.
6. With reference to the Central Excise Rules, 2002, comment on the following taking into account the position as on 15.04.2007:
 - (i) E-payment of excise duty is mandatory for the assessee who has deposited Rs.50 lakh or more as excise duty in cash for the financial year 2006-07.
 - (ii) The Deputy or Assistant Commissioner of Central Excise can remit the duty payable between Rs.1,000 to Rs.2,500.
 - (iii) Mr. A issues an excise duty invoice without delivery of goods mentioned therein. Mr. A shall not be liable to any penalty.
 - (iv) For the purposes of payment of duty, the expressions 'duty' or 'duty of excise' also include the amount payable in terms of the CENVAT Credit Rules, 2004.
7. With reference to the CENVAT Credit Rules, 2004, discuss whether the following are true or false taking into account the position as on 15.04.2007:
 - (i) It is compulsory for all kind of service providers providing taxable as well as exempted services and not maintaining separate input/input services credit accounts to utilize CENVAT credit only to the extent of 20% of service tax payable on taxable output service.
 - (ii) CENVAT credit can be taken only if all the particulars required under the Central Excise Rules, 2002 or Service Tax Rules, 1994 are contained in the duty paying document.
 - (iii) It is necessary for the manufacturer of excisable goods to take all reasonable steps to ensure that the input or capital goods in respect of which he has taken the CENVAT credit are goods on which the appropriate excise duty as indicated in the accompanying documents has been paid by the manufacturer of such input or capital goods.
 - (iv) Mr.B takes CENVAT credit on inputs received for use in the production of final products manufactured by him. However, the said final product gets exempted absolutely under section 5A of the Central Excise Act, 1944. Accordingly, Mr.B has to pay an amount equivalent to the CENVAT credit in respect of the inputs lying in stock or in process or contained in the final product lying in stock.

8. With reference to rule 12CC of the Central Excise Rules, 2002, explain the provisions relating to imposition of restrictions on a manufacturer, first stage and second stage dealer or an exporter.
9. Can a manufacturer remove excisable goods manufactured by him for carrying out a process not amounting to manufacture to any other premises, without payment of duty? Discuss.
10. Write a brief note on effect of amendments etc. of rules, notifications or orders under section 38A of the Central Excise Act, 1944.
11. Briefly explain the following with reference to the Customs Act, 1962:

- (i) Goods
- (ii) Conveyance

12. A product is liable to 16% basic excise duty. However, a notification has granted exemption to the said product whereby the rate of basic excise duty has been reduced from 16% to 8%. Further, a special excise duty @ 5% is also leviable on such product by virtue of a Finance Act. This product has been imported by 'Y' from Brazil. Basic customs duty is leviable @ 8%.

You have to determine the rate of additional duty of customs (CVD) leviable, if any, on such product.

13. 'X' imported capital goods during the period April-May 2005 under the Project Import scheme and deposited Rs.50,00,000 as security deposit. The goods were cleared after provisional assessment. However, as per the final assessment order dated 13.08.2005, the duty worked out to be only Rs.10,00,000. Accordingly, 'X' became entitled to refund and a refund order of Rs.40,00,000 was issued on 31.01.2006. The cheque of the said amount was issued to 'X' on 06.02.2006. As regards, the amount of Rs.10,00,000 retained by the department, a challan was prepared on 09.02.2006, but the said amount was actually credited to the Government Treasury only on 12.02.2006.

Subsequently, on 09.08.2006, a show cause notice was issued to 'X' on the ground that the audit party has observed that the capital goods imported by 'X' were not the capital goods eligible for Project Import Scheme.

'X' contends that the show cause notice is time barred as the limitation period of 6 months under section 28 of the Customs Act commenced from 07.02.2006 i.e., after the cheque was issued and there was nothing further to be adjusted. However, the Customs Department claims that the relevant date of adjustment of duty for the purpose of computing the limitation period under section 28 of the Customs Act would be the date on which the duty amount of Rs.10,00,000 was actually credited to the Government Treasury. Therefore, period of 6 months would commence from 13.02.2006.

Give your views on the situation with the help of a decided case law, if any.

14. When can the transaction value be accepted under rule 4(2) of the Customs Valuation (Determination of Price of Imported Goods) Rules, 1988? Discuss.
15. Write a note on power of the Central Board of Excise and Customs to make regulations under section 84 of the Customs Act, 1962.
16. State the circumstances under which goods are considered to have been removed improperly from a warehouse under the Customs Act, 1962.
17. Explain briefly the provisions regarding drawback allowable on re-export of duty paid goods as such.
18. (i) Explain whether the infrastructural support services provided by ABX Ltd. shall be liable to service tax.
(ii) Discuss whether service provided by a money changer in relation to exchange of foreign currency is a forex broking service chargeable to service tax under 'banking and other financial services'.

- (iii) Mr. Ajay, a chartered accountant represents his client Mr. Vijay in a case relating to evasion of income-tax before the Income-tax Appellate Tribunal. Mr. Ajay charges Rs.25,000 as consideration for this service. Discuss whether Mr. Ajay is liable to pay service tax on such service.
- 19. With reference to the Service Tax Rules, 1994, discuss the procedures and facilities for a large tax payer.
- 20. Write short notes on:
 - (a) Registrar to an issue's services
 - (b) Public relations services

SUGGESTED ANSWERS/HINTS

1. (a) According to section 2(a) of the Central Excise Act, 1944, adjudicating authority means any authority competent to pass any order or decision under this Act, but does not include the Central Board of Excise and Customs constituted under the Central Boards of Revenue Act, 1963, Commissioner of Central Excise (Appeals) or Appellate Tribunal.
 - (b) According to section 2(k) of the Central Excise Act, 1944, wholesale dealer means a person who buys or sells excisable goods wholesale for the purpose of trade or manufacture, and includes a broker or commission agent who, in addition to making contracts for the sale or purchase of excisable goods for others, stocks such goods belonging to others as an agent for the purpose of sale.
 2. Section 37E (w.e.f. 13.07.2006) inserted by the Taxation Laws (Amendment) Act, 2006 provides for publishing the name of any person and particulars of any proceedings in relation to such person, in public interest. The provisions are:
 - (1) The Central Government may publish name of any person and any other particulars relating to any proceedings or prosecution in respect of such person if it is of the opinion that it is necessary or expedient in the public interest to do so. The Government can do the publication in such manner as it thinks fit.
 - (2) The publication shall be made in relation to any penalty only after the time for presenting an appeal to the Commissioner (Appeals) or to the Appellate Tribunal expires without an appeal being presented or the appeal, if presented, gets disposed of.
 - (3) In the case of a firm, company or other association of persons, the names of the partners of the firm, directors, managing agents, secretaries and treasurers or managers of the company, or the members of the association, as the case may be, may also be published if, in the opinion of the Central Government, circumstances of the case justify it.
 3. The facts of the case are similar to the case of CCEx. v. Illpea Paramount Pvt. Ltd. 2006 (204) ELT 22 (P & H). In this case, the High Court observed that section 11AC leaves no room for discretion in the quantum of penalty to be imposed. Section 11AC inter alia provides that where any duty of excise has not been levied or paid or has been short-levied or short-paid or erroneously refunded by reasons of fraud, collusion or any wilful mis-statement or suppression of facts, or contravention of any of the provisions of this Act or of the rules made thereunder with intent to evade payment of duty, the person who is liable to pay duty as determined under sub-section (2) of section 11A, shall also be liable to pay a penalty equal to the duty so determined.
- The High Court observed that if the situation demanded penalty, the same had to be equal to the amount of duty. The High Court categorically stated that penalty was not to be levied mechanically. The statute itself laid down that penalty was to be levied only where duty was short-levied or short-paid or erroneously refunded by reason of "fraud, collusion or any wilful misstatement or suppression of facts, or contravention of any of the provisions of this Act or of the rules." The High Court explained that the element of mens rea has been statutorily insisted upon.

Therefore, the High Court held that once mens rea has been established, the quantum is not left to the discretion of the authority.

Thus, CESTAT is not right in reducing the amount of penalty.

4. With effect from 01.04.2007, a new rule 10A has been inserted in the Central Excise Valuation (Determination of Excisable Goods) Rules, 2000 vide Notification No. 9/2007 CE (NT) dated 01.03.2007 to provide for valuation in case of job-work. The rule provides that where goods are manufactured by a job-worker on behalf of a person (commonly known as principal manufacturer), the value for payment of excise duty would be based on the sale value at which the principal manufacturer sells the goods, as against the present provision where the value is taken as cost of raw material plus the job charges.

The rule lays down that where the excisable goods are produced or manufactured by a job-worker, on behalf of a person (hereinafter referred to as principal manufacturer), then,-

- (i) in a case where the goods are sold by the principal manufacturer for delivery at the time of removal of goods from the factory of job-worker, where the principal manufacturer and the buyer of the goods are not related and the price is the sole consideration for the sale, the value of the excisable goods shall be the transaction value of the said goods sold by the principal manufacturer.
- (ii) in a case where the goods are not sold by the principal manufacturer at the time of removal of goods from the factory of the job-worker, but are transferred to some other place from where the said goods are to be sold after their clearance from the factory of job-worker and where the principal manufacturer and buyer of the goods are not related and the price is the sole consideration for the sale, the value of the excisable goods shall be the normal transaction value of such goods sold from such other place at or about the same time and, where such goods are not sold at or about the same time, at the time nearest to the time of removal of said goods from the factory of job-worker.
- (iii) in a case not covered under clause (i) or (ii), the provisions of foregoing rules, wherever applicable, shall mutatis mutandis apply for determination of the value of the excisable goods.

The cost of transportation, if any, from the premises, wherefrom the goods are sold, to the place of delivery shall not be included in the value of excisable goods.

Here, job-worker means a person engaged in the manufacture or production of goods on behalf of a principal manufacturer, from any inputs or goods supplied by the said principal manufacturer or by any other person authorised by him.

5. Section 35F of the Central Excise Act provides that person desirous of appealing against an order shall, pending the appeal, deposit the duty demanded or penalty levied. However, the appellate authority is empowered to grant stay/waiver of such pre-deposit if it is of the opinion that the deposit of duty or penalty will cause undue hardship to such person.

The Supreme Court in the case of Benara Valves Ltd. v. CCEX. 2006 (204) ELT 513 (SC) has observed that prima facie case alone is not enough for passing an interim order granting stay/waiver of pre-deposit. However, if the sustainability of the demand itself is in doubt, stay could be granted. The Supreme Court stated that the petition for stay should not be disposed of in routine manner without thinking of the consequences flowing from the order requiring deposit of full or part of demand. The Apex Court elaborated that there could be no rule of universal application in such matters and order should be passed keeping in view the factual scenario involved.

The Supreme Court explained that merely because it has indicated some principles to grant stay/waiver of pre-deposit through its decisions in various case laws, orders which are not sustainable on grounds of fairness, legality and public interest cannot be passed. Where denial of interim relief may lead to public mischief, grave irreparable private injury or shake citizen's faith in the impartiality of public administration, interim relief can be given.

Further, the Apex Court stated that mere assertion of the undue hardship is not sufficient; it has to be established by the applicant for obtaining stay of pre-deposit. Undue hardship is related to economic hardship. The Supreme Court explained that word undue adds something more than just hardship. It means an excessive hardship or a hardship greater than the circumstances warrant.

6. (i) With effect from 01.04.2007, Notification No. 8/2007 CE (NT) dated 01.03.2007 has made e-payment mandatory for payment of duty by all assesseees who have paid excise duty of Rs.50 lakh or more in cash during the preceding financial year. This has been done by adding a third proviso in rule 8(1).
- (ii) Rule 21 has been amended vide Notification No. 8/2007 CE (NT) dated 01.03.2007 so as to increase the power of remission given to various officers of central excise. The Deputy/Assistant Commissioner of Central Excise is now empowered to remit the duty payable between Rs.10,000 to Rs.1,00,000. Earlier this range was Rs.1,000 to Rs.2,500.
- (iii) A new sub-rule (2) has been inserted in rule 26 vide Notification No. 8/2007 CE (NT) dated 01.03.2007 to provide for penal action against the person who issues:
 - (i) excise duty invoice without delivery of goods mentioned therein or abets in making such invoice; or
 - (ii) any other document or abets in making such document,

on the basis of which the user of said invoice or document is likely to take or has taken any ineligible benefits like CENVAT credit or refund.

Such person shall be liable to a penalty not exceeding the amount of such benefit or Rs.5,000 whichever is greater.

Hence, Mr. A shall be liable to penalty.
- (iv) An explanation has been inserted after rule 8(4) vide Notification No. 8/2007 CE (NT) dated 01.03.2007 to provide that for the purposes of payment of duty, the expressions 'duty' or 'duty of excise' shall also include the 'amount' payable in terms of the CENVAT Credit Rules, 2004. Therefore, all 'amounts' payable (like payment under rule 6(3) of the CENVAT Credit Rules, 2004 etc.) should be paid along with duty payable by 5th or 15th of the next month.
7. (i) False. Clause (d) has been inserted in rule 6(3) vide Notification No. 10/2007 CE (NT) dated 01.03.2007 so as to provide an option to general insurance service providers providing taxable as well as exempted insurance services and not maintaining separate input/input services credit accounts to utilise CENVAT credit proportionate to the inputs and input services used in providing taxable services. Earlier such service provider could utilise the credit only to the extent of 20% of service tax payable on taxable output service.

The scheme is optional and is subject to fulfillment of certain conditions. The scheme has come into effect from 1st April, 2007. It may be noted that the scheme is applicable only to general insurance services referred to in section 65(105)(d) of the Finance Act, 1994.

- (ii) True. Sub-rule (2) of rule 9 has been amended vide Notification No. 10/2007 CE (NT) dated 01.03.2007 to provide that CENVAT credit can be taken only if all the particulars as prescribed under the Central Excise Rules, 2002 or the Service Tax Rules, 1994 are available on the invoice or other duty-paying document.

However, the Deputy/Assistant Commissioner of Central Excise may allow the CENVAT credit even if the said document does not contain all the particulars but contains certain specified information and the Deputy/Assistant Commissioner is satisfied that the goods or services covered by the said document have been received and accounted for in the books of the accounts of the receiver.

- (iii) False. Sub-rule (3) of rule 9 which prescribed the above-mentioned treatment has been omitted vide Notification No. 10/2007 CE (NT) dated 01.03.2007. With the deletion of the above said rule, it implies that, now, the person availing CENVAT credit is not responsible to

ensure that duty paid to manufacturer of inputs or capital goods has been deposited by such manufacturer.

- (iv) True. Notification No. 10/2007 CE (NT) dated 01.03.2007 has inserted new sub-rule (3) in rule 11 to provide that a manufacturer shall be required to pay an amount equivalent to the CENVAT credit in respect of inputs received for use in the manufacture of the final product which is lying in stock or in process or is contained in the final product lying in stock, if,-

- (i) he opts for exemption from the whole of the excise duty leviable on the said final product under a notification issued under section 5A of the Central Excise Act; or
- (ii) the said final product has been exempted absolutely under section 5A of the Act.

If after deducting the said amount from the balance of CENVAT credit (if any lying in his credit) there still remains a balance, it shall lapse. Such balance shall not be allowed to be utilized for payment of duty on any other final product whether cleared for home consumption or for export, or for payment of service tax on any output service, whether provided in India or exported.

8. Rule 12CC provides for power to impose restrictions in certain types of cases. It empowers the Central Government to provide for certain measures including restrictions on a manufacturer, first stage and second stage dealer or an exporter. The Central Government can exercise such powers where having regard to the extent of evasion of duty, nature and type of offences or any other relevant factors, it is of the opinion that in order to prevent evasion and default in payment of excise duty, it is necessary in the public interest to impose restrictions. The nature of restrictions, (e.g. suspension of registration in case of a dealer) types of facilities to be withdrawn and procedure for issue of such order by an officer authorized by the Board may be specified by a notification in the Official Gazette. The provisions of this rule shall not be subject to anything contained in the Central Excise Rules, 2002.

9. Rule 16C of the Central Excise Rules, 2002 provides that the Commissioner may allow a manufacturer to remove excisable goods manufactured by him for carrying out test or any process not amounting to manufacture to any other premises without payment of duty. The said other premises may be registered or unregistered. After such tests or any such other process are carried out, the Commissioner may allow,-

- (a) bringing back of such goods to the said factory without payment of duty, for subsequent clearance for home consumption or export, as the case may be, or
- (b) removal of such goods from the said other premises, for home consumption on payment of duty leviable thereon or without payment of duty for export, as the case may be.

However, this rule shall not apply to the goods known as "prototypes" which are sent out for trial or development test.

10. Where any rule, notification or order made or issued under the Central Excise Act or any notification or order issued under such rule, is amended, repealed, superseded or rescinded, then, unless a different intention appears, such amendment, repeal, supersession or rescinding shall not:

- (a) revive anything not in force or existing at the time at which the amendment, repeal, supersession or rescinding takes effect; or
- (b) affect the previous operation of any rule, notification or order so amended, repealed, superseded or rescinded or anything duly done or suffered thereunder; or
- (c) affect any right, privilege, obligation or liability acquired, accrued or incurred under any rule, notification or order so amended, repealed, superseded or rescinded; or
- (d) affect any penalty, forfeiture or punishment incurred in respect of any offence committed under or in violation of any rule, notification or order so amended, repealed, superseded or rescinded; or

- (e) affect any investigation, legal proceeding or remedy in respect of any such right, privilege, obligation, liability, penalty, forfeiture or punishment as aforesaid,
and any such investigation, legal proceeding or remedy may be instituted, continued or enforced and any such penalty, forfeiture or punishment may be imposed as if the rule, notification or order, as the case may be, had not been amended, repealed, superseded or rescinded.

11. (i) As per section 2(22) of the Customs Act, 1962 'goods' includes-

- (a) vessels, aircrafts and vehicles;
- (b) stores;
- (c) baggage;
- (d) currency and negotiable instruments;
- (e) any other kind of movable property.

- (ii) As per section 2(9) of the Customs Act, 1962 conveyance is defined to include a vessel, an aircraft and a vehicle. As the Customs Act seeks to consolidate the laws relating to levy of duties on import and export of goods, it is necessary to cover all the modes of transport. Therefore, the Act uses the term conveyance with an inclusive definition covering all the 3 modes of transport i.e., water, air and land. The specific terms are: vessel (by sea), aircraft (by air) and vehicle (by land).

12. Section 3(1) of the Customs Tariff Act, 1975 provides that any article which is imported into India shall, in addition, be liable to a duty equal to the excise duty for the time being leviable on a like article if produced or manufactured in India. This duty shall be called as additional duty (CVD). If such excise duty on a like article is leviable at any percentage of its value, the additional duty to which the imported article shall be so liable shall be calculated at that percentage of the value of the imported article.

Since, the CVD should be equal to the excise duty for the time being leviable on a like article if produced or manufactured in India, therefore, the rate of CVD will be 8% basic excise duty (effective rate after exemption) and 5% special excise duty.

Special excise duty levied by the Finance Act would also be considered for computing the rate of CVD as the Supreme Court in the case of J.K. Synthetics Ltd. v. Union of India 2006 (204) ELT 369 (Del.) has held that the purpose of levying CVD would be defeated if the rate had to be restricted to basic excise duty when the local manufacturers have to compulsorily pay the special excise duty as well. If special excise duty is not considered while levying CVD, the CVD so levied would not counterbalance the excise duty payable by the local manufacturers on a like product in order to ensure a level playing field.

The Supreme Court elaborated that the expression "excise duty for the time being leviable" is not qualified by any word which limits the excise duty to be payable only under the Central Excise Act, 1944. In other words, it can also include a special duty of excise payable in terms of the Finance Act.

13. Section 28(3)(b) inter alia provides that the relevant date for issuing show cause notice in a case where duty is provisionally assessed under section 18 is the date of adjustment of duty after the final assessment thereof. The facts of the given case are similar to the case of Gujarat Alkalies & Chemicals Ltd. v. CCus. (Import) 2006 (204) ELT 237 (Bom.) wherein the High Court has observed that as per section 18(2)(a) of the Customs Act, 1962, the excess or shortfall in duty is determined only after the finally assessed duty is adjusted from the provisionally paid duty. It is only after such adjustment, the obligation to make good the deficiency or entitlement for refund arises.

The High Court explained that issuing the refund cheque and crediting the duty amount equivalent to the duty finally assessed into the Government Treasury are the two steps to be taken after the adjustment of duty. It was held by the High Court that the relevant date of adjustment of duty would be the date on which the refund cheque is issued or the date on which the amount is

credited into the Government Treasury, whichever is earlier. Thus, where the proper officer in implementation of the refund order issues the refund cheque first and then credits the duty amount into the Government Treasury, then, the relevant date of adjustment of duty would be the date on which the refund cheque is issued. Similarly, if the amount of duty is credited into the Government Treasury first and thereafter the refund cheque is issued, then, the relevant date of adjustment of duty would be the date on which the amount is credited into the Government Treasury.

Therefore, in the given case since the refund cheque is issued before (06.02.2006) the duty amount is credited into the Government treasury (12.02.2006), the date of issue of refund cheque i.e. 06.02.2006 would be the relevant date of adjustment of duty thus making the show cause notice time barred.

14. The transaction value can be accepted under rule 4(2) of the Customs Valuation (Determination of Price of Imported Goods) Rules, 1988 if:
 - (a) the sale is in the ordinary course of trade under fully competitive conditions;
 - (b) the sale does not involve any abnormal discount or reduction from the ordinary competitive price;
 - (c) the sale does not involve special discounts limited to exclusive agents;
 - (d) objective and quantifiable data exist with regard to the adjustments required to be made, under the provisions of rule 9, to the transaction value;
 - (e) there are no restrictions as to the disposition or use of the goods by the buyer other than restrictions which —
 - (i) are imposed or required by law or by the public authorities in India; or
 - (ii) limit the geographical area in which the goods may be resold; or
 - (iii) do not substantially affect the value of the goods;
 - (f) the sale or price is not subject to some condition or consideration for which a value cannot be determined in respect of the goods being valued;
 - (g) no part of the proceeds of any subsequent resale, disposal or use of the goods by the buyer will accrue directly or indirectly to the seller, unless an appropriate adjustment can be made in accordance with the provisions of Rule 9 of these rules; and
 - (h) the buyer and seller are not related.
15. Section 84 empowers the Board to make regulations providing for
 - (a) the form and manner in which an entry may be made in respect of any specified class of goods imported or to be exported by post, other than goods which are accompanied by a label or declaration containing the description, quantity and value thereof;
 - (b) the examination, assessment to duty, and clearance of goods imported or to be exported by post;
 - (c) the transshipment or transit of goods imported by post from one Customs station to another or to a place outside India.
16. Section 72 of the Customs Act provides that in any of the following circumstances the goods shall be considered to have been removed improperly from a warehouse –
 - (a) where any warehoused goods are removed from a warehouse in contravention of section 71 of the Customs Act;
 - (b) where any warehoused goods have not been removed from a warehouse at the expiration of the period during which such goods are permitted under section 61 to remain in a warehouse;
 - (c) where any warehoused good have been taken under section 64 as samples without payment of duty;

- (d) where any goods in respect of which a bond has been executed under section 59 and which have not been cleared for home consumption or exportation are not duly accounted for to the satisfaction of the proper officer.
17. For allowing duty drawback on re-export of duty paid goods, sub-section (1) of section 74 of the Customs Act, 1962 provides that:
- (i) the goods should have been imported into India;
 - (ii) the import duty should have been paid thereon;
 - (iii) the goods should be capable of being easily identified as the goods, which were originally imported;
 - (iv) the goods should have been entered for export either on a shipping bill through sea or air or on a bill of export through land, or as baggage, or through post and the proper officer, after proper examination of the goods and after ensuring that there is no prohibition or restriction on their export, should have permitted clearance of such goods for export;
 - (v) the goods should have been identified to the satisfaction of the Assistant or Deputy Commissioner of Customs as the goods, which were imported, and
 - (vi) the goods should have been entered for export within two years from the date of payment of duty on the importation thereof.

However, in any particular case, the aforesaid period of two years may, on sufficient cause being shown, be extended by the Board by such further period, as it may deem fit. Once these conditions are satisfied, then 98% of the import duty paid on such goods at the time of importation shall be repaid as drawback.

18. (i) With effect from 01.05.2006, business support services have been made chargeable to service tax vide Finance Act, 2006 under sub-clause (zzzq) of clause (105) of section 65 of the Finance Act, 1994. Business support services inter alia include infrastructural support services. Thus, with effect from 01.05.2006 infrastructural support services provided by ABX Ltd. shall be liable to service tax.
- (ii) Service tax is leviable on foreign exchange (forex) broking service under the category of 'banking and other financial service'. In terms of the provisions of the Finance Act, 1994, foreign exchange broker includes a money changer (authorized dealer of foreign exchange). Circular No. 92/3/2007 ST dated 12.03.2007 has clarified that 'money changing' and 'foreign exchange broking' are two distinct activities. Money changing is an activity of sale and purchase of foreign exchange at the prevalent market rates. On the other hand, foreign exchange broking is the activity performed as an intermediary, on a commission/brokerage basis, for facilitating the clients who wish to buy or sell foreign exchange. The foreign exchange broker providing foreign exchange broking service does not hold title to the foreign exchange. Accordingly, service tax is not leviable on money changing per se, as such activity does not fall under the category of foreign exchange broking.
- (iii) Any service provided to a client by a chartered accountant in his professional capacity is liable to service tax under section 65(105)(s) of the Finance Act, 1994. However, Notification No. 25/2006 ST dated 13.07.2006 has exempted the taxable services provided or to be provided inter alia by a practising chartered accountant in his professional capacity, to a client, relating to representing the client before any statutory authority in the course of proceedings initiated under any law for the time being in force, by way of issue of notice, from the whole of service tax leviable thereon.

In the given case, Mr. Ajay is representing his client Mr. Vijay before the Income-tax Appellate Tribunal, a statutory authority. Thus, in view of the above-mentioned exemption notification Mr. Ajay shall not be liable to pay service tax on the services rendered by him.

19. Notification No. 28/2006 ST dated 30.09.2006 has inserted rule 10 after Rule 9 in the Service Tax Rules, 1994. Rule 10 lays down the procedure and facilities for the large taxpayer. This has been done to incorporate the concept of large taxpayer in the service tax provisions.

The provisions of this rule are discussed below:

Notwithstanding anything contained in these rules, the following shall apply to a large taxpayer, -

- (1) A large taxpayer shall submit the returns, as prescribed under these rules, for each of the registered premises. A large taxpayer who has obtained a centralized registration under rule 4(2) shall submit a consolidated return for all such premises.
 - (2) A large taxpayer, on demand, may be required to make available the financial, stores and CENVAT credit records in electronic media, such as, compact disc or tape for the purposes of carrying out any scrutiny and verification, as may be necessary.
 - (3) A large taxpayer may, with intimation of at least 30 days in advance, opt out to be a large taxpayer from the first day of the following financial year.
 - (4) Any notice issued but not adjudged by any of the Central Excise Officer administering the Act or rules made thereunder immediately before the date of grant of acceptance by the Chief Commissioner of Central Excise, Large Taxpayer Unit, shall be deemed to have been issued by Central Excise Officers of the said unit.
 - (5) Provisions of these rules, in so far as they are not inconsistent with the provisions of this rule shall mutatis mutandis apply in case of a large taxpayer.
20. (a) With effect from 01.05.2006, services provided by a registrar to an issue have been made liable to service tax by the Finance Act, 2006.

Section 65(105)(zzzi) of the Finance Act, 1994 defines the taxable service of registrar to an issue as any service provided or to be provided to any person, by a registrar to an issue, in relation to sale or purchase of securities.

Section 65(89c) of the Finance Act, 1994 provides that registrar to an issue means any person carrying on the activities in relation to an issue including collecting application forms from investors, keeping a record of applications and money received from investors or paid to the seller of securities, assisting in determining the basis of allotment of securities, finalising the list of persons entitled to allotment of securities and processing and despatching allotment letters, refund orders or certificates and other related documents.

As per section 65(59a) of the Finance Act, 1994 issue means an offer of sale or purchase of securities to, or from, the public or the holder of securities.

- (b) With effect from 01.05.2006, public relations services have been made liable to service tax by the Finance Act, 2006.

Section 65(105)(zzzs) of the Finance Act, 1994 defines the taxable public relations service as any service provided or to be provided to any person, by any other person, in relation to managing the public relations of such person, in any manner.

Section 65(86c) of the Finance Act, 1994 provides that public relations includes strategic counselling based on industry, media and perception research, corporate image management, media relations, media training, press release, press conference, financial public relations, brand support, brand launch, retail support and promotions, events and communications and crisis communications.

IMPORTANT AMENDMENTS MADE BETWEEN 01.05.2006 TO 30.04.2007

Students may note that the Study Material for Indirect taxes contains all the relevant amendments made by the Finance Act, 2006. Further, Circulars/Notifications issued up to 30.04.2006 have also been incorporated therein. The following are the amendments which have been made till 30.04.2007.

It may carefully be noted that for the students appearing in November 2007 the amendments made by Notifications, Circulars and other legislations up to 30.04.2007, as detailed hereunder, are relevant.

A. CENTRAL EXCISE

(i) Amendments by the Taxation Laws (Amendment) Act, 2006

The Taxation Laws (Amendment) Bill was enacted on 13.07.2006, the date on which it received the assent of the President. It has made certain amendments in the Central Excise Act, 1944 with the object of rationalizing and simplifying procedures, widening of tax base and plugging loopholes leading to leakage of revenue.

All the amendments made by the Taxation Laws (Amendment) Act, 2006 have come into effect from 13.07.2006.

Amendments in the Central Excise Act, 1944

1. Adjudication proceedings to conclude in respect of a person who voluntarily deposits the full excise duty demanded along with interest and penalty equal to 25% of the excise duty [Section 11A(1A)]
 - (i) Section 11A(1) provides that where excise duty is short/not levied or short/not paid or erroneously refunded, the Central Excise Officer can issue a show cause notice within 1 year from the relevant date. However, this period of 1 year is extended to 5 years when such short/non levy or short/non payment or erroneous refund of excise duty is by reason of fraud, collusion, or any wilful mis-statement or suppression of facts, or contravention of any of the provisions of the Central Excise Act or the rules made thereunder with an intent to evade payment of excise duty.
 - (ii) A new sub-section (1A) has been inserted after sub-section (1) in section 11A. The new sub-section provides an option to the person or his agent to whom a notice has been served by the Central Excise Officer for short/non levy or short/non payment or erroneous refund of excise duty by reason of fraud, collusion, or any wilful mis-statement or suppression of facts, or contravention of any of the provisions of the Central Excise Act or the rules made thereunder with an intent to evade payment of excise duty.
 - (iii) Such person or his agent may pay the excise duty in full or in part as may be accepted by him, including the interest payable thereon under section 11AB and penalty equal to 25% of the excise duty specified in the notice or the excise duty so accepted by such person within 30 days of the receipt of the notice.
 - (iv) Further, a proviso has been inserted in sub-section (2) of section 11A. Sub-section (2) provides that the Central Excise Officer shall consider the representation, if any, made by the person on whom a notice under sub-section (1) is served. He shall determine the amount of excise duty due from such person and thereupon such person shall pay the amount so determined. However, such amount shall not exceed the amount specified in the notice.
 - (v) The newly inserted proviso lays down that where such person has paid the excise duty in full together with interest and penalty, the proceedings in respect of such person and other persons to whom notices (referred to in point 1) have been served shall be deemed to have been concluded in respect of the matters stated therein. The proceedings shall conclude notwithstanding anything contained in sections 9, 9A and 9AA.
 - (vi) Another proviso has been inserted in sub-section (2). This proviso lays down that in cases where such person has paid excise duty in part along with interest and penalty, the Central Excise Officer shall determine the amount of excise duty or interest which will not exceed the amount partly due from such person.
2. Commissioner to direct any Central Excise Officer subordinate to him to apply to the Commissioner (Appeals) [Section 35E(2)]

Section 35E(2) of the Central Excise Act gives powers to Commissioner of Central Excise to pass certain orders. The Commissioner of Central Excise may of its own motion, call for and examine

the record of any proceeding in which an adjudicating authority subordinate to him has passed any order so as to satisfy itself upon the legality or propriety of the order. Thereafter, the Commissioner may direct such authority to apply to the Commissioner (Appeals) to determine such points as may be specified by it.

The Taxation Laws (Amendment) Act, 2006 has amended section 35E(2) to the effect that now the Commissioner may also direct any Central Excise Officer subordinate to him (apart from the adjudicating authority subordinate to him which has passed the order) to apply to the Commissioner (Appeals) to determine such points as may be specified by it.

3. Property may be attached provisionally to protect revenue in certain cases [New section 11DDA]

A new section 11DDA has been inserted by the Taxation Laws (Amendment) Act, 2006. The provisions of this section are:

- (1) During the pendency of any proceeding under section 11A or section 11D, the Central Excise Officer may provisionally attach any property belonging to the person on whom notice is served under sub-section (1) of section 11A or sub-section (2) of section 11D, as the case may be, in accordance with the rules made in this behalf under section 142 of the Customs Act, 1962.
- (2) Such an attachment shall be done only when the Central Excise Officer is of the opinion that the attachment is necessary for the purpose of protecting the interests of revenue. However, a previous approval of the Commissioner of Central Excise, by order in writing, is a prerequisite for such provisional attachment.
- (3) Such an attachment can be done for a period of 6 months. This period will commence from the date of the order of the Commissioner of Central Excise permitting such provisional attachment.
- (4) However, this period may be extended by the Chief Commissioner of Central Excise by such further period or periods as he thinks fit. The reasons for such an extension shall be recorded in writing. It is to be noted that the total period of extension in any case shall not exceed 2 years.
- (5) If an application for settlement of a case under section 32E is made to the Settlement Commission, the period commencing from the date on which such an application is made and ending with the date on which an order under section 32F(1) is made shall be excluded from the extended period mentioned in point (4).

4. Information in respect of persons in certain cases to be published [New section 37E]

This new section, added by the Taxation Laws (Amendment) Act, 2006 provides for publishing the name of any person and particulars of any proceedings in relation to such person, in public interest. The provisions are discussed below in detail:

- (1) The Central Government may publish name of any person and any other particulars relating to any proceedings in respect of such person if it is of the opinion that it is necessary or expedient in the public interest to do so. The Government can do the publication in such manner as it thinks fit.
- (2) The publication shall be made in relation to any penalty only after the time for presenting an appeal to the Commissioner (Appeals) or the Appellate Tribunal expires without an appeal being presented or the appeal, if presented, gets disposed of.
- (3) In the case of a firm, company or other association of persons, the names of the partners of the firm, directors, managing agents, secretaries and treasurers or managers of the company, or the members of the association, as the case may be, may also be published if, in the opinion of the Central Government, circumstances of the case justify it.

(ii) Significant amendments made through Notifications/Circulars issued between 01.05.2006 and 30.04.2007

1. Following amendments have been made in the Central Excise Rules, 2002:

- (i) With effect from 01.04.2007, e -payment has been made mandatory for payment of duty by all assessees who have paid excise duty of rupees 50 lakh or more in cash during the preceding financial year. This has been done by adding a third proviso in rule 8(1) [Notification No. 8/2007 CE (NT) dated 01.03.2007].
- (ii) In rule 8, sub-rule (3A) has been substituted vide Notification No. 13/2006 CE (NT) dated 01.06.2006. The new sub-rule provides that if the assessee defaults in payment of duty beyond 30 days from the due date then he shall pay excise duty for each consignment at the time of removal, without utilizing the CENVAT credit. He shall continue to pay duty consignment-wise (from PLA) till the date he pays the outstanding amount including interest thereon. In the event of any failure, it shall be deemed that such goods have been cleared without payment of duty and the consequences and penalties as provided in these rules shall follow.

The old sub-rule provided that the assessee would lose the facility to pay the duty in monthly instalments if he made a default in payment of duty by due date and the same is discharged beyond a period of 30 days from the due date. This forfeiture would start from the date of communication of the order passed by the Assistant/Deputy Commissioner of Central Excise in this regard. The forfeiture of the facility would continue for a period of two months or till such date on which all dues including interest thereof are paid, whichever is later. Further, during this period the assessee would not be able to utilize the CENVAT credit for the payment of duty on final products. He would compulsorily pay the excise duty for each consignment by debit to the account current and in the event of any failure, it would be deemed that such goods have been cleared without payment of duty and the consequences and penalties as provided in these rules would follow.

Thus, the requirement of the order passed by the Assistant/Deputy Commissioner and limitation of period of 2 months for paying consignment-wise duty has been done away with in the new sub-rule.

- (iii) An explanation has been inserted after rule 8(4) to provide that for the purposes of payment of duty, the expressions 'duty' or 'duty of excise' shall also include the 'amount' payable in terms of the CENVAT Credit Rules, 2004. Therefore, all 'amounts' payable (like payment under rule 6(3) of the CENVAT Credit Rules, 2004 etc.) should be paid along with duty payable by 5th or 15th of the next month [Notification No. 8/2007 CE (NT) dated 01.03.2007].
- (iv) With effect from 01.04.2007, an invoice, apart from containing other prescribed particulars, shall also contain address of the jurisdictional Central Excise Division. This has been done by amending sub-rule (2) of rule 11 [Notification No. 8/2007 CE (NT) dated 01.03.2007].
- (v) Notification No. 03/2007-CE (NT) dated 08.02.2007 has inserted a proviso before the existing proviso in rule 12(1). The proviso lays down that an assessee, manufacturing pan masala falling under tariff item 2106 90 20 or pan masala containing tobacco falling under tariff item 2403 99 90, shall also file a statement along with the monthly return. The statement shall contain the monthly summary of-
 - (i) the purchase invoices for the month with the names and addresses of the suppliers of betel nut, tobacco and packing material along with the quantity of the said goods purchased; and
 - (ii) the sales invoices for the month with the names and addresses of the buyers, description, quantity and value of goods sold by the assessee.

In cases where the goods are not sold from the factory, the address of the premises to

which the goods are dispatched from the factory shall also be provided.

- (vi) Notification No. 30/2006-CE (NT) dated 30.12.2006 has inserted a new rule 12CC after rule 12C. The new rule provides for power to impose restrictions in certain types of cases.

Rule 12CC empowers the Central Government to provide for certain measures including restrictions on a manufacturer, first stage and second stage dealer or an exporter. The Central Government can exercise such powers where having regard to the extent of evasion of duty, nature and type of offences or any other relevant factors, it is of the opinion that in order to prevent evasion and default in payment of excise duty, it is necessary in the public interest to impose restrictions. The nature of restrictions, (e.g. suspension of registration in case of a dealer) types of facilities to be withdrawn and procedure for issue of such order by an officer authorized by the Board may be specified by a notification in the Official Gazette. The provisions of this rule shall not be subject to anything contained in Central Excise Rules, 2002.

- (vii) Notification No. 26/2006-CE (NT) dated 28.12.2006 has substituted rule 16C which prescribes special procedure for removal of excisable goods for carrying out tests with a new rule. The new rule prescribes special procedure for removal of excisable goods for carrying out certain processes.

New rule 16C provides that the Commissioner may allow a manufacturer to remove excisable goods manufactured by him for carrying out test or any process not amounting to manufacture to any other premises without payment of duty. The said other premises may be registered or unregistered. After such tests or any such other process are carried out, the Commissioner may allow-

- (a) bringing back of such goods to the said factory without payment of duty, for subsequent clearance for home consumption or export, as the case may be, or
- (b) removal of such goods from the said other premises, for home consumption on payment of duty leviable thereon or without payment of duty for export, as the case may be:

However, this rule shall not apply to the goods known as "prototypes" which are sent out for trial or development test.

In order to ensure uniformity in the conditions to be imposed by the Commissioner, it has been clarified vide Circular No. 844/02/2007-CX dated 31.01.2007 that the procedure prescribed under sub-rules (2),(3),(4) & (9) of rule 12AA of the Central Excise Rules, 2002 should broadly be followed in such cases. However, proper records of receipt of goods, its use, nature of activities carried out, goods processed and cleared by the said other premises should be maintained. Further, any waste/scrap arising at such other premises while carrying out the test/other processes should either be cleared on payment of duties or it should be returned back.

- (viii) Rule 21 has been amended to increase the power of remission given to various officers of central excise.

- (a) The Superintendent is now empowered to remit the duty payable up to Rs.10,000. Earlier this limit was Rs.1,000.
- (b) The Deputy/Assistant Commissioner is now empowered to remit the duty payable between Rs.10,000 to Rs.1,00,000. Earlier this range was Rs.1,000 to Rs.2,500.
- (c) The Additional/Joint Commissioner is now empowered to remit the duty payable between Rs.1,00,000 to Rs.5,00,000. Earlier this range was Rs.2,500 to Rs.5,000 [Notification No. 8/2007 CE (NT) dated 01.03.2007].

- (ix) Rule 25 inter alia provides for a penalty, on any producer, manufacturer, registered person of a warehouse or a registered dealer, of Rs.10,000 or the duty payable on the excisable goods in respect of which any of the specified contravention have been committed, whichever is greater.

Rule 26 inter alia provides that any person who acquires possession of, or is in any way concerned in transporting, removing, depositing etc. any excisable goods which he knows or has reason to believe are liable to confiscation shall be liable to a penalty not exceeding the duty on such goods or Rs.10,000 whichever is greater.

With effect from 11.05.2007, rule 25 and 26 have been amended to reduce the minimum penalty from the present level of Rs.10,000 to Rs.2,000 [Notification No. 8/2007 CE (NT) dated 01.03.2007].

- (x) A new sub-rule (2) has been inserted in rule 26 to provide for penal action against the person who issues:

- (i) excise duty invoice without delivery of goods mentioned therein or abets in making such invoice; or
- (ii) any other document shipping bill, bill of lading, etc. or abets in making such document, on the basis of which the user of said invoice or document is likely to take or has taken any ineligible benefits like CENVAT credit or refund.

Such person shall be liable to a penalty not exceeding the amount of such benefit or Rs.5,000 whichever is greater [Notification No. 8/2007 CE (NT) dated 01.03.2007].

2. Following amendments have been made in the CENVAT Credit Rules, 2004:

- (i) The definition of capital goods provided in rule 2(a) has been amended to the effect that in place of goods falling under "heading No.68.02 and sub-heading No.6801.10", the goods falling under "heading 6805, grinding wheels and the like, and parts thereof falling under heading 6804" would qualify to be the capital goods. Consequently, in rule 4(2)(b) also the goods falling under heading No. 68.02 and sub-heading No. 6801.10 have been substituted with the goods falling under heading 6805, grinding wheels and the like, and parts thereof falling under heading 6804 [Notification No. 07/2007 CE (NT) dated 21.02.2007].
- (ii) Rule 3(7)(c) has been amended to provide that CENVAT credit of the additional duty of Customs to the extent of Rs.30 per square meter shall be allowed in case of marble slabs or tiles falling under tariff items 2515 12 20 and 2515 12 90 respectively. Earlier such credit was allowed in case of marble slabs or tiles falling under sub-heading No. 2504.21 or 2504.31 respectively [Notification No. 07/2007 CE (NT) dated 21.02.2007].
- (iii) A new rule 5A has been inserted after rule 5 vide Notification No. 24/2007 CE (NT) 25.04.2000. New rule 5A is in relation to refund of CENVAT credit to units in specified areas. The new rule provides that the Central Government may allow refund of CENVAT credit of duty taken on inputs used in the manufacture of final products cleared in terms of Notification No.20/2007-CE dated 25.04.2007 if the manufacturer is unable to utilize such credit for paying duty on such final products.

However, the refund shall not be allowed if the final products are exempt or subject to nil rate of duty. The refund of credit shall be allowed subject to such procedure, conditions and limitations, as may be specified by notification.

For the purposes of this rule, "duty" means the duties specified in sub-rule (1) of rule 3 of these rules.

Notification No.20/2007 CE dated 25.04.2007 has granted exemption to certain specified goods cleared from a unit located in the States of Assam or Tripura or Meghalaya or Mizoram or Manipur or Nagaland or Arunachal Pradesh or Sikkim from so much of the duty of excise leviable thereon as is equivalent to the amount of duty

paid by the manufacturer of goods other than the amount of duty paid by utilization of CENVAT credit under the CENVAT Credit Rules, 2004.

- (iv) Rule 6(3)(a) enlists certain exempted goods in respect of which a manufacturer, who produces dutiable and exempted goods from common inputs or input services and does not maintain separate accounts for the same, has to pay an amount equivalent to the CENVAT credit attributable to the inputs and input services used in, or in relation to, the manufacture of such goods at the time of their clearance from the factory. The following amendments have been made in the exempted goods mentioned in that list:
 - (a) In place of goods falling within heading 22.04 of the First Schedule to the Central Excise Tariff Act, now such list shall cover goods falling within heading 2207 of the First Schedule to the Central Excise Tariff Act. Item (i) of such list has been amended to give effect to this amendment. Heading 2207 covers ethyl alcohol and other spirits, denatured of any strength.
 - (b) In place of newsprint, in rolls or sheets, falling within heading No. 48.01 of the First Schedule now such list shall cover newsprint, in rolls, sheets or reels, falling within Chapter 48. Item (v) of such list has been amended to give effect to this amendment. Chapter 48 covers paper and paperboards and articles thereof etc. [Notification No. 07/2007 CE (NT) dated 21.02.2007].
- (v) Clause (d) has been inserted in rule 6(3) to provide an option to general insurance service providers providing taxable as well as exempted insurance schemes and not maintaining separate input/input services credit accounts to utilise CENVAT credit proportionate to the inputs and input services used in providing taxable services. Earlier such service provider could utilise the credit only to the extent of 20% of service tax payable on taxable output service.

The scheme is optional and is subject to fulfillment of certain conditions. The scheme has come into effect from 1st April, 2007. It may be noted that the scheme is applicable only to general insurance services referred to in section 65(105)(d). The conditions subject to which full credit, attributable to inputs/input services used in providing taxable services, can be utilised are:

- (i) While exercising this option, the output service provider shall intimate his option in writing to the Superintendent of Central Excise giving the following particulars, namely:-
 - (a) name and address of the provider of output service;
 - (b) date from which this option is exercised or proposed to be exercised;
 - (c) description of taxable services;
 - (d) description of exempted services;
 - (e) CENVAT credit of inputs and input services lying in balance as on the date of exercising the option under this condition.
- (ii) The option given under part (i) for a financial year shall not be withdrawn during the remaining part of the financial year.
- (iii) The output service provider shall-
 - (a) determine, provisionally, the amount equivalent to CENVAT credit attributable to exempted services, in the following manner, namely:-

$$\text{CENVAT credit attributable to exempted services (provisional)} = (A/B) \times C,$$
 where
 $A = \text{Total value of exempted services provided during the preceding financial year}$
 $B = \text{Total value of taxable and exempted services provided during the}$

preceding financial year

C = Total CENVAT credit of inputs and input services taken during the month

- (b) pay the amount attributable to exempted services determined as above for each month, on or before 5th day of the following month.
 - (c) determine the CENVAT credit attributable to exempted services for the whole financial year in the following manner, namely:-

$$\text{CENVAT credit attributable to exempted services} = (X/Y) \times Z,$$

where

X = total value of exempted services provided during the financial year

Y = total value of taxable and exempted services provided during the financial year

Z = total CENVAT credit of inputs and input services taken during the financial year
 - (d) pay an amount equal to the difference between the amount determined as per item (c) and the amount determined as per item (a), on or before the 30th June of the succeeding financial year, where the amount determined as per item (c) is more than the amount paid.
 - (e) in addition to the amount short-paid, be liable to pay interest @ 24% from the due date i.e. 30th June till the date of payment, where the amount short-paid is not paid within the said due date.
 - (f) where the amount determined as per item (c) is less than the amount determined and paid as per item (a), adjust the excess amount on his own, by taking credit of such amount.
- (iv) The output service provider shall intimate to the jurisdictional Superintendent of Central Excise, within a period of 15 days from the date of such payment or adjustment, the following particulars, namely:-
- (a) month-wise details of CENVAT credit attributable to exempted services for the whole financial year, determined provisionally as per part (iii) item (a)
 - (b) the amount equivalent to CENVAT credit attributable to exempted services, determined provisionally for each month and paid month-wise as per part (iii) item(b)
 - (c) CENVAT credit attributable to exempted services for the whole financial year determined as per part (iii) item (c)
 - (d) amount short paid determined as per part (iii) item (d), alongwith the date of payment of the amount short paid
 - (e) interest payable and paid, if any, on the amount short paid, determined as per part (iii) item (e), and
 - (f) credit taken on account of excess payment, if any, determined as per part (iii) item (f)
- (v) Where the amount equivalent to CENVAT credit attributable to exempted services cannot be determined provisionally since no taxable general insurance service has been provided, the output service provider is not required to provisionally determine and pay CENVAT credit attributable to exempted services for each month. In such a case he shall determine the CENVAT credit attributable to exempted services for the whole year as prescribed in part (iii) item (c) and pay the amount so calculated on or before 30th June of the succeeding financial year.

(vi) Where the amount determined under part (v) is not paid within the said due date i.e. the 30th June, the output service provider shall, in addition to the said amount, be liable to pay interest @ 24% per annum from the due date till the date of payment [Notification No. 10/2007 CE (NT) dated 01.03.2007].

- (vi) Sub-rule (2) of rule 9 provides that CENVAT credit cannot be denied if basic prescribed details are available on the duty paying document even though all the particulars required under the rules are not mentioned therein.

Sub-rule (2) of rule 9 has been amended vide Notification No. 10/2007 CE (NT) dated 01.03.2007 to provide that the CENVAT credit can be taken only if all the particulars as prescribed under the Central Excise Rules, 2002 or the Service Tax Rules, 1994 are available on the invoice or other duty-paying document.

However, the Deputy/Assistant Commissioner may allow the CENVAT credit even if the said document does not contain all the particulars but the following two conditions are satisfied:

- (a) The document contains the following information:

- details of duty or service tax payable,
- description of the goods or taxable service,
- assessable value,
- central excise/service tax registration number of the person issuing the invoice (inserted vide Notification No. 19/2007 CE (NT) dated 09.03.2007)
- name and address of the factory or warehouse or premises of first or second stage dealers or provider of taxable service, and

- (b) The Deputy/Assistant Commissioner is satisfied that the:

- (i) goods or services covered by the said document have been received and
- (ii) accounted for in the books of the account of the receiver.

- (vii) Sub-rule (3) of rule 9 provides that the manufacturer or provider of output service or the input service distributor should take all reasonable steps to ensure that the input or capital goods or input service in respect of which he has taken the CENVAT credit are goods or services on which the appropriate duty of excise or service tax as indicated in the accompanying documents has been paid by the manufacturer of such input or capital goods or the provider of input service as the case may be.

Sub-rule (3) of rule 9 has been omitted vide Notification No. 10/2007 CE (NT) dated 01.03.2007. With the deletion of the above said rule, it implies that, now, the person availing CENVAT credit is not responsible to ensure that duty or service tax paid to manufacturer of inputs or capital goods or provider of input service respectively has been deposited by such person. However, such person is required to fulfill other obligations specified under CENVAT Credit Rules, 2004 like maintenance of records etc.

- (viii) Consequent amendments have been made in sub-rules (1) and (3) of rule 15 which prescribe a penalty inter alia where CENVAT credit in respect of input or capital goods or input service has been taken without taking reasonable steps to ensure that appropriate excise duty or service tax as indicated in the duty paying document has been deposited with the department.

Now, after the deletion of sub-rule (3) of rule 9 no penalty shall be imposed if credit is taken without taking reasonable steps to ensure that appropriate excise duty or service tax has been deposited with the department [Notification No. 10/2007 CE (NT) dated 01.03.2007].

(ix) Sub-rule (11) has been inserted after sub-rule (10) in rule 9 so as to allow the output service provider or the input service distributor to rectify mistakes or omission and file revised return within 60 days from the date of filing of original return [Notification No. 10/2007 CE (NT) dated 01.03.2007].

(x) New sub-rule (3) has been inserted in rule 11 to provide that a manufacturer shall be required to pay an amount equivalent to the CENVAT credit in respect of inputs received for use in the manufacture of the final product which is lying in stock or in process or is contained in the final product lying in stock, if,-

(i) he opts for exemption from the whole of the excise duty leviable on the said final product under a notification issued under section 5A of the Central Excise Act; or

(ii) the said final product has been exempted absolutely under section 5A of the Act.

If after deducting the said amount from the balance of CENVAT credit (if any lying in his credit) there still remains a balance, it shall lapse. Such balance shall not be allowed to be utilized for payment of duty on any other final product whether cleared for home consumption or for export, or for payment of service tax on any output service, whether provided in India or exported [Notification No. 10/2007 CE (NT) dated 01.03.2007].

(xi) Similar amendment has been made in respect of cases wherein taxable services become exempted. New sub-rule (4) has been inserted in rule 11 to provide that a output service provider shall be required to pay an amount equivalent to the CENVAT credit, if any, taken by him in respect of inputs received for providing the said service and is lying in stock or is contained in the taxable service pending to be provided, when he opts for exemption from payment of whole of the service tax leviable on such taxable service.

After deducting the said amount from the balance of CENVAT credit (if any lying in his credit) if there still remains a balance, it shall lapse. Such balance shall not be allowed to be utilized for payment of duty on any excisable goods, whether cleared for home consumption or for export or for payment of service tax on any other output service, whether provided in India or exported.

It should be noted that in this case reversal of credit of input services is not required [Notification No. 10/2007 CE (NT) dated 01.03.2007].

(xii) Notification No. 31/2006 CE (NT) dated 30.12.2006 has inserted a new rule 12AA after rule 12A which provides for the power to impose restrictions in certain types of cases.

Rule 12AA empowers the Central Government to provide for certain measures including restrictions on a manufacturer, first stage and second stage dealer or an exporter if there is a misuse of CENVAT credit. The Central Government can exercise such powers where having regard to the extent of misuse of CENVAT credit, nature and type of such misuse and any other relevant factors, it is of the opinion that in order to prevent the misuse of the provisions of CENVAT credit, it is necessary in the public interest to impose restrictions. The nature of restrictions, (e.g. restrictions on utilization of CENVAT credit and suspension of registration in case of a dealer) types of facilities to be withdrawn and procedure for issue of such order by an officer authorized by the Board may be specified by a notification in the Official Gazette. The provisions of this rule shall not be subject to anything contained in CENVAT Credit Rules, 2004.

(xiii) The minimum penalty prescribed in rule 15 for wrongly taking CENVAT credit on inputs/capital goods/input services or for contravening any of the provisions of the rules has been reduced from Rs.10,000 to Rs.2,000. Sub-rule (1) and sub-rule (3) have been amended to give effect to this change. This amendment has come into effect from 11.05.2007 [Notification No. 10/2007 CE (NT) dated 01.03.2007].

- (xiv) Rule 3(1) and 3(7)(b) have been amended to allow credit of secondary and higher education cess for payment of education cesses [Notification No. 10/2007 CE (NT) dated 01.03.2007].
3. Notification No. 25/2007 CE (NT) dated 25.04.2007 has prescribed the following procedure for claiming refund of unutilised CENVAT credit under rule 5A:
- (a) The manufacturer shall file a declaration with the jurisdictional Assistant/Deputy Commissioner describing the finished goods proposed to be manufactured, rate of duty thereof, manufacturing or processing formula and quantity and quality of the materials actually used. The declaration shall also contain the tariff classification, rate of duty paid or payable on the materials so used in relation to the finished goods to be manufactured and cleared. However, if any particulars given in the declaration have undergone any changes, the revised declaration shall be filed by the manufacturer;
 - (b) The manufacturer shall submit a statement containing details namely quantity of opening balance of inputs, quantity of inputs received during the month, value thereof, duty paid or payable thereon, amount of CENVAT credit taken, quantity of inputs used during the month, quantity of final products manufactured, quantity of inputs lying in stock at the end of the month, amount of CENVAT credit utilised for payment of duty on the final product and amount of CENVAT credit lying in balance to the Assistant/Deputy Commissioner by the 7th day of the next month for claiming refund;
 - (c) The Assistant/Deputy Commissioner after appropriate verification may refund the balance amount of unutilised credit, if any, at the end of the month under consideration to the manufacturer within a period of 3 months from the date of receipt of the statement; and
 - (d) If there is likely to be any delay in the verification, the Assistant/Deputy Commissioner shall refund 80% of the amount on provisional basis by the 30th day of the month following the month under consideration.

The above-mentioned conditions shall be subject to the conditions prescribed in Notification No. 20/2007 CE dated 25.04.2007.

4. In pursuance of rule 12CC of the Central Excise Rules, 2002, and rule 12AA of the CENVAT Credit Rules, 2004, the Central Government vide Notification No. 32/2006 CE (NT) dated 30.12.2006 has declared that an officer authorised by the Board may order for withdrawal of facilities or impose restrictions where a manufacturer, first stage or second stage dealer, or an exporter including a merchant exporter is prima facie found to be knowingly involved in any of the following, -
- (a) removal of goods without the cover of an invoice and without payment of duty;
 - (b) removal of goods without declaring the correct value for payment of duty, where a portion of sale price, in excess of invoice price, is received by him or on his behalf but not accounted for in the books of account;
 - (c) taking of CENVAT credit without the receipt of goods specified in the document based on which the said credit has been taken;
 - (d) taking of CENVAT credit on invoices or other documents which a person has reasons to believe as not genuine;
 - (e) issue of excise duty invoice without delivery of goods specified in the said invoice;
 - (f) claiming of refund or rebate based on the excise duty paid invoice or other documents which a person has reason to believe as not genuine.

Facilities to be withdrawn and imposition of restrictions:

The officer authorized by the Board may impose following restrictions in case of a manufacturer involved in committing any of the above-mentioned offences:

- (i) the facility of monthly payment of duties may be withdrawn and the assessee shall be

required to pay excise duty for each consignment at the time of removal of goods;

- (ii) payment of duty by utilisation of CENVAT credit may be restricted and the assessee shall be required to pay excise duty without utilising the CENVAT credit.

It may be noted that the person against whom the order for withdrawal of facilities or imposition of restrictions has been passed may continue to take CENVAT credit but he would not be able to utilize the credit for payment of duty during the period specified in the said order.

Further, where a person is found to be knowingly involved in committing any one or more type of the above-mentioned offences for the second time or subsequently, every removal of goods from his factory may be ordered to be under an invoice which shall be countersigned by the Inspector of Central Excise or the Superintendent of Central Excise before the said goods are removed from the factory or warehouse. For second time or subsequent offence, the restriction specified in clauses (i) and (ii) may also be imposed.

Where a first stage or second stage dealer is found to be knowingly involved in committing the type of offence specified at clauses (d) or (e), the registration granted under rule 9 of the Central Excise Rules 2002 may be suspended for a specified period. During the period of suspension, the said dealer shall not issue any Central Excise Invoice. However, he may continue his business and issue sales invoices without showing excise duty in the invoice and no CENVAT credit shall be admissible to the recipient of goods under such invoice.

Where a merchant exporter is found to be knowingly involved in committing the type of offence specified at clause (f), the self sealing facility for export consignment may be withdrawn whereby each export consignment shall be examined and sealed by the jurisdictional Central Excise Officer.

Further, any other facility available to a manufacturer, first stage or second stage dealer or an exporter provided by a circular or an order issued by the Board may also be ordered to be withdrawn for a specified period.

Monetary limit:

The provisions of this notification shall be applicable only in a case where the duty or CENVAT credit alleged to be involved in the above-mentioned offences is more than Rs.10 lakhs.

Procedure:

The Commissioner of Central Excise or Additional Director General of Central Excise Intelligence, as the case may be, after examination of records and other evidence, and after satisfying himself that the person has knowingly committed the above-mentioned offence, may forward a proposal to the Chief Commissioner or Director General of Central Excise Intelligence, as the case may be, specifying the facilities to be withdrawn and restriction to be imposed and the period of such withdrawal or restrictions, within 30 days of the detection of the case, as far as possible.

The Chief Commissioner of Central Excise or Director General of Central Excise Intelligence, as the case may be, shall examine the said proposal and after satisfying himself that the records and evidence relied upon in the said proposal are sufficient to form a reasonable belief that a person has knowingly committed the said offences, may forward the proposal along with his recommendations to the Board. However, the Chief Commissioner of Central Excise or Director General of Central Excise Intelligence, before forwarding his recommendations, shall give an opportunity of being heard to the person against whom the proceedings have been initiated and shall take into account any representation made by such person before he forwards his recommendations to the Board.

An officer authorized by the Board shall examine the recommendations received from the Chief Commissioner of Central Excise or Director General of Central Excise Intelligence and issue an order specifying the type of facilities to be withdrawn or type of restrictions

imposed, along with the period for which said facilities will not be available or the period for which the restrictions shall be operative.

The Board has authorized Member (Central Excise), Central Board of Excise and Customs to issue such orders.

5. With effect from 01.04.2007, a new rule 10A has been inserted in the Central Excise Valuation (Determination of Price of Excisable Goods) Rules, 2000 vide Notification No. 9/2007 CE (NT) dated 01.03.2007 to provide for valuation in case of job-work. The rule provides that where goods are manufactured by a job-worker on behalf of a person (commonly known as principal manufacturer), the value for payment of excise duty would be based on the sale value at which the principal manufacturer sells the goods, as against the present provision where the value is taken as cost of raw material plus the job charges.

The rule lays down that where the excisable goods are produced or manufactured by a job-worker, on behalf of a person (hereinafter referred to as principal manufacturer), then, -

- (i) in a case where the goods are sold by the principal manufacturer for delivery at the time of removal of goods from the factory of job-worker, where the principal manufacturer and the buyer of the goods are not related and the price is the sole consideration for the sale, the value of the excisable goods shall be the transaction value of the said goods sold by the principal manufacturer.
- (ii) in a case where the goods are not sold by the principal manufacturer at the time of removal of goods from the factory of the job-worker, but are transferred to some other place from where the said goods are to be sold after their clearance from the factory of job-worker and where the principal manufacturer and buyer of the goods are not related and the price is the sole consideration for the sale, the value of the excisable goods shall be the normal transaction value of such goods sold from such other place at or about the same time and, where such goods are not sold at or about the same time, at the time nearest to the time of removal of said goods from the factory of job-worker.
- (iii) in a case not covered under clause (i) or (ii), the provisions of foregoing rules, wherever applicable, shall mutatis mutandis apply for determination of the value of the excisable goods.

The cost of transportation, if any, from the premises, wherefrom the goods are sold, to the place of delivery shall not be included in the value of excisable goods.

Here, job-worker means a person engaged in the manufacture or production of goods on behalf of a principal manufacturer, from any inputs or goods supplied by the said principal manufacturer or by any other person authorised by him.

6. The assesseees who pay less than Rs.100 lakh as excise duty from account current during the financial year to which the Annual Financial Information Statement relates were exempted from filing of such annual information return vide Notification No. 35/2004-CE (N.T.) dated 01.11.2004. Notification No.17/2006 CE (NT) dated 01.08.2006 has rescinded the above-mentioned notification and has extended the benefit of exemption of not filing Annual Information Return to Indian Ordnance Factories, Department of Defence Production and Ministry of Defence while keeping intact the exemption in case of assesseees who pay excise duty of less than 100 lakh rupees from account current during the financial year to which Annual Financial Information Statement relates.
7. Notification No. 8/2003 CE dated 01.03.2003 has been amended vide Notification No.45/2006 CE dated 20.11.2006 to provide that account books, registers, writing pads and file folders falling under heading 4820 or 4821 of the First Schedule of the Central Excise Tariff shall be entitled to small scale exemption even if they bear a brand name or trade name whether registered or not, of another person. Prior to this amendment, such goods were not entitled to small scale exemption if they bore a brand name of another person.
8. Notification No.5/2006 CE (NT) dated 14.03.2006 which lays down conditions to be fulfilled in order to obtain refund under rule 5 of the CENVAT Credit Rules, 2004 has been amended

vide Notification No. 13/2007 CE(NT) dated 01.03.2007. In order to claim refund the manufacturer inter alia has to submit an application to the jurisdictional Deputy/Assistant Commissioner along with the original shipping bill or bill of export duly certified by the officer of customs. Now after the amendment the manufacturer can also submit a photocopy of the shipping bill/bill of export attested by the customs officer along with the application.

9. With effect from 01.04.2007, exemption limit under the SSI scheme has been increased from Rs.1 crore to Rs.1.5 crore.
10. Circular No. 843/1/2007-CX dated 17.01.2007 has clarified that the provisions of Standards of Weight & Measures (Packaged Commodities) Rules, 1977 shall apply in case of bulk sale of ice cream in packages to hotel/catering industry etc. and accordingly, the assessee is required to declare the retail sale price on such packages.

LARGE TAX PAYER UNITS

The Finance Minister in his Budget Speech 2005-06 announced the proposal to set up Large Taxpayer Units (hereinafter referred to as LTUs) in the country in line with the international practice, which would service large taxpayers paying excise duty, corporate tax/income-tax and service tax under a single window. LTU is a trade facilitative measure seeking to address and deliver appropriate solutions to the unique compliance issues that may arise. The establishment of LTU is a step to achieve excellence in the formulation and implementation of Service Tax and Excise initiatives by creating a climate for voluntary compliance by providing guidance and building of mutual trust. It is envisaged that this approach will improve India's business climate, and will reassure the trade that their taxation related concerns would be dealt with in a fair and transparent manner.

The Government has decided to implement the LTU scheme in a phased manner. The first Large Taxpayer Unit has been set up at Bangalore. LTUs will also be established in a phased manner in Chennai, Delhi, Kolkata, and Mumbai. The Chief Commissioner, Central Excise and Service Tax will head the LTU in Bangalore.

Conceptually, LTU is a self-contained tax office that provides single point interface with the tax administration to the large taxpayers who pay direct and indirect taxes above the threshold limit as specified in the Notification No. 20/2006 C.E (NT) dated 30.09.2006 (discussed in point 3 later). It is a single office that would deal with central excise/service tax/ income tax/ corporate tax issues of all units holding a single PAN. Once a taxpayer acquires the status of LTU, the entire jurisdiction of central excise, service tax and income tax matters shall stand transferred to the said LTU in respect of all his manufacturing units, service providing premises, and other registered premises located throughout the country. Some of such activities are as given below: -

- (a) Filing of returns
- (b) Filing of refund/rebate claims
- (c) Audit, Adjudication and Appeals
- (d) Filing of intimation, permissions
- (e) Visit to units
- (f) Acceptance of proof of export

A LTU will be headed by a Chief Commissioner (either from CBDT or from CBEC). The Chief Commissioner, LTU is expected to undertake following functions-

- (a) overall administration of LTU;
- (b) co-ordination between the direct tax and the indirect tax wings of LTU;
- (c) distribution of work amongst the LTU officers;
- (d) monitoring of revenue collection;
- (e) quality Assurance Checks/ taxpayer feedback system;
- (f) devising effective taxpayer assistance system;
- (g) review of the orders passed by the Commissioners as adjudicating authority (as a member of Review Committee);

- (h) issuance of trade notices/ circulars to bring about uniformity in tax administration as well as determination of amount of tax payable;
- (i) coordination with the Boards (CBEC and CBDT), Directorates and with other field formations in the matters such as audit verification, revenue recoveries, etc.

The Chief Commissioner, LTU will intimate the jurisdictional Central Excise, Service Tax and Income Tax Commissioners regarding the transfer of the specified units from their jurisdiction to the LTU. There will be Commissioners posted in LTU, who would be holding executive and appellate charges. The powers and duties would be similar to that of other field commissioners. However, they are required to play a pro-active role in ensuring the fulfilment of objectives of a LTU. The Commissioners of Direct and Indirect Taxes are expected to work in a coordinated manner. Other Group 'A', 'B', 'C' officers along with supporting staff will be posted by CBDT and CBEC. The Chief Commissioner, LTU will assign a Client Executive for each taxpayer from among the Additional/Joint/Deputy/Asstt. Commissioner posted in LTU, and the said Client Executive will be the single point interface with the large taxpayer for all purposes.

The officers posted in LTU will have all India jurisdiction in respect of all registered premises of a large taxpayer registered in that particular LTU. The erstwhile Central Excise or Service Tax Commissionerate Officers will have concurrent jurisdiction. However, the interaction with these units will be limited to specific functions requiring physical presence of the officers for purposes as warehousing, sealing or any other work as assigned by the LTU.

1. Following amendments have been made in the Central Excise Rules, 2002 vide Notification No. 18/2006 CE (NT), dated 30.09.2006 so as to incorporate the concept of large tax payer.

- (i) In rule 2, after sub-rule (e), another sub-rule has been inserted to define "large taxpayer" as a person who-

- (i) has one or more registered premises under the Central Excise Act, 1944; or
- (ii) has one or more registered premises under Chapter V of the Finance Act, 1994;

and is an assessee under the Income Tax Act, 1961, who holds a Permanent Account Number issued under section 139A of the said Act, and satisfies the conditions and observes the procedures as notified by the Central Government in this regard.

- (ii) Rule 12BB has been inserted after Rule 12AA which lays down the procedure and facilities for the large taxpayer. The provisions of this rule are:

- (1) A large taxpayer may remove excisable goods (intermediate goods), except motor spirit, commonly known as petrol, high speed diesel and light diesel oil without payment of duties of excise under the cover of a transfer challan or invoice from any of his registered premises (sender premises) where such goods are produced, manufactured or warehoused to his other registered premises (recipient premises) for further use in the manufacture or production of such other excisable goods (subject goods). However, the large taxpayer cannot remove the intermediate goods without payment of duty to the premises of a first or second stage dealer. The removal of intermediate goods without payment of duty from the sender premises to recipient premises shall be subject to the conditions that-

- (a) the subject goods are manufactured using the said intermediate goods and cleared on payment of appropriate duties of excise leviable thereon within a period of 6 months, from the date of receipt of the intermediate goods in the recipient premises; or
- (b) the subject goods are manufactured using the said intermediate goods and exported out of India, under bond or letter of undertaking within a period of 6 months, from the date of receipt of the intermediate goods in the recipient premises,

and that any other conditions prescribed by the Commissioner of Central Excise, Large Taxpayer Unit in this regard are satisfied.

The transfer challan or invoice shall be serially numbered and shall contain the registration number, name, address of the large taxpayer, description, classification, time and date of removal, mode of transport and vehicle registration number, quantity of the goods and registration number and name of the consignee.

However, if the subject goods manufactured or produced using the said intermediate goods are not cleared on payment of appropriate duties of excise leviable thereon or are not exported out of India within the said period of 6 months, duties of excise payable on such intermediate goods shall be paid by the recipient premises with interest in the manner and rate specified under section 11AB. The duty payable shall be the duty payable on the date and time of removal of the intermediate goods from the sender's premises. If the large taxpayer fails to pay such amount, it shall be recovered along with interest in the same manner as provided under section 11A and section 11AB.

Illustration 1

Excise duty is payable on intermediate goods, namely, electronics goods, manufactured by factory A which are removed without payment of duties of excise for use in the manufacture of subject goods, namely, machines, in factory B of the large taxpayer. In case such machines are not exported or are removed without payment of duties of excise, then factory B shall pay duties of excise payable on the electronic goods so cleared along with interest.

Further, if any duty of excise is payable on such intermediate goods and if the said duty is not payable on such subject goods, the said duty of excise as equivalent to the total amount payable on such intermediate goods along with interest under section 11AB of the Act shall be paid by the recipient premises. The duty payable shall be the duty payable on the date and time of removal of the intermediate goods from the sender's premises. If the large taxpayer fails to pay such amount, it shall be recovered along with interest in the same manner as provided under section 11A and section 11AB respectively of the Act.

Illustration 2

National Calamity Contingent duty is payable on intermediate goods namely, polyester yarn manufactured by factory A. Such yarn is removed without payment of duty of excise for use in the manufacture of subject goods, namely, grey fabrics in factory B of a large taxpayer, (on which such National Calamity Contingent duty is not payable), then factory B shall pay an amount equivalent to the National Calamity Contingent duty that would have been payable on the polyester yarn along with interest under section 11AB of the Act.

It may be noted that the provisions of this sub-rule shall not be applicable if the recipient premises is availing following notifications:

- (i) No. 32/99-CE, dated 08.07.1999;
- (ii) No. 33/99-CE, dated 08.07.1999;
- (iii) No. 39/2001-CE, dated 31.07.2001;
- (iv) No. 56/2002-CE, dated 14.11.2002;
- (v) No. 57/2002-CE, dated 14.11.2002;
- (vi) No. 56/2003-CE, dated 25.06.2003; and
- (vii) No. 71/2003-CE, dated 09.09.2003

Also, the provisions of this sub-rule shall not apply in respect of a EOU or a unit located in a EHTP or STP.

- (2) Where a registered premises of a large taxpayer manufacturing excisable goods has paid to the credit of Central Government any duty of excise in excess of duty of excise

payable on account of arithmetical error, the said large taxpayer may adjust the excess duty so paid by him, against his duty liability for the subsequent period subject to the limitations prescribed under rule 3(7)(b) of the CENVAT Credit Rules, 2004.

However, such adjustment shall be admissible only if the said registered premises has not passed on the incidence of such excess duty so paid to any other person, and the consignee does not avail credit of such duty under the CENVAT Credit Rules, 2004.

- (3) Any notice issued but not adjudged by any of the Central Excise Officer immediately before the date of grant of acceptance by the Chief Commissioner of Central Excise, Large Taxpayer Unit, shall be deemed to have been issued by Central Excise officers of the said Unit.
 - (4) A large taxpayer shall submit the monthly returns, as prescribed under these rules, for each of the registered premises.
 - (5) A large taxpayer, on demand, may be required to make available the financial, production, stores and CENVAT credit records in electronic media, such as, compact disc or for the purposes of carrying out any scrutiny and verification as may be necessary.
 - (6) A large taxpayer may, with intimation of at least 30 days in advance, opt out to be a large taxpayer from the first day of the following financial year.
 - (7) The provisions of other rules of Central Excise Rules, 2002 in so far as they are not inconsistent with the provisions of this rule shall mutatis mutandis apply in case of a large taxpayer.
2. Following amendments have been made in CENVAT Credit Rules, 2004 vide Notification No. 19/2006 CE (NT), dated 30.09.2006 so as to incorporate the concepts of large tax payer.
- (i) In rule 2, sub-rule (na) has been renamed as sub-rule (naa) so that sub-rule (na) can define "large taxpayer" to have the meaning assigned to it in the Central Excise Rules, 2002.
 - (ii) Rule 12A has been inserted after Rule 12 in the CENVAT Credit Rules, 2004 which lays down the procedure and facilities for the large taxpayer. The provisions of rule 12A are as under:
 - (1) A large taxpayer may remove inputs (except motor spirit, commonly known as petrol, high speed diesel and light diesel oil) or capital goods, as such, on which CENVAT credit has been taken without payment of an amount specified in rule 3(5) of the CENVAT Credit Rules, 2004 under the cover of a transfer challan or invoice from any of his registered premises (sender premises) to his other registered premises (recipient premises) other than a premises of a first or second stage dealer for further use in the manufacture or production of final products in the recipient premises. Such removal shall be subject to the conditions that-
 - (a) the final products are manufactured or produced using the said inputs and cleared on payment of appropriate duties of excise leviable thereon within a period of 6 months, from the date of receipt of the inputs in the recipient premises; or
 - (b) the final products are manufactured or produced using the said inputs and exported out of India, under bond or letter of undertaking within a period of 6 months, from the date of receipt of the inputs in the recipient premises,
 and that any other conditions prescribed by the Commissioner of Central Excise, Large Taxpayer Unit in this regard are satisfied.

The transfer challan or invoice shall be serially numbered and shall contain the registration number, name, address of the large taxpayer, description, classification, time and date of removal, mode of transport and vehicle registration number, quantity of the goods and registration number and name of the consignee.

However, if the final products manufactured or produced using the said inputs are not

cleared on payment of appropriate duties of excise leviable thereon or are not exported out of India within the said period of 6 months from the date of receipt of the input goods in the recipient premises, or such inputs are cleared as such from the recipient premises, an amount equal to the credit taken in respect of such inputs by the sender premises shall be paid by the recipient premises with interest in the manner and rate specified under rule 14 of these rules. The first recipient premises may take CENVAT credit of such amount paid by it as if it was a duty paid by the sender premises who removed such goods on the basis of a document showing payment of such duties.

Also, if such capital goods are used exclusively in the manufacture of exempted goods, or such capital goods are cleared as such from the recipient premises, an amount equal to the credit taken in respect of such capital goods by the sender premises shall be paid by the recipient premises with interest in the manner and rate specified under rule 14 of these rules.

If a large taxpayer fails to pay any of such amount, it shall be recovered along with interest in the manner as provided under rule 14 of these rules.

It may be noted that the provisions of this sub-rule shall not be applicable if the recipient premises is availing following notifications:

- (i) No. 32/99-CE, dated 08.07.1999;
- (ii) No. 33/99-CE, dated 08.07.1999;
- (iii) No. 39/2001-CE, dated 31.07.2001;
- (iv) No. 56/2002-CE, dated 14.11.2002;
- (v) No. 57/2002-CE, dated 14.11.2002;
- (vi) No. 56/2003-CE, dated 25.06.2003; and
- (vii) No. 71/2003-CE, dated 09.09.2003

Also, the provisions of this sub-rule shall not apply in respect of an EOU or a unit located in a EHTP or STP.

- (2) CENVAT credit of the specified duties taken by a sender premises shall not be denied or varied in respect of any inputs or capital goods, removed as such under sub-rule (1) on the ground that the said inputs or the capital goods have been
 - (i) removed without payment of an amount specified in rule 3(5) of these rules; or
 - (ii) used in the manufacture of any intermediate goods removed without payment of duty under sub-rule (1) of rule 12BB of Central Excise Rules, 2002.

For the purpose of this sub-rule intermediate goods shall have the same meaning assigned to it in sub-rule (1) of rule 12BB of the Central Excise Rules, 2002.

- (3) A large taxpayer may transfer CENVAT credit available with one of its registered manufacturing premises or premises providing taxable service to its other registered premises by,-
 - (i) making an entry for such transfer in the records maintained under rule 9;
 - (ii) issuing a transfer challan containing registration number, name and address of the registered premises transferring the credit as well as receiving such credit, the amount of credit transferred and the particulars of such entry as mentioned in clause (i),

and such recipient premises can take CENVAT credit on the basis of such transfer challan as mentioned in clause (ii):

It may be noted that such transfer or utilisation of CENVAT credit shall be subject to the limitations prescribed under rule 3(7)(b).

It may be noted that the provisions of this sub-rule shall not be applicable if the

registered manufacturing premises is availing following notifications:

- (i) No. 32/99-CE, dated 08.07.1999;
 - (ii) No. 33/99-CE, dated 08.07.1999;
 - (iii) No. 39/2001-CE, dated 31.07.2001;
 - (iv) No. 56/2002-CE, dated 14.11.2002;
 - (v) No. 57/2002-CE, dated 14.11.2002;
 - (vi) No. 56/2003-CE, dated 25.06.2003; and
 - (vii) No. 71/2003-CE, dated 09.09.2003
- (4) A large taxpayer shall submit a monthly return, as prescribed under these rules, for each of the registered premises.
 - (5) Any notice issued but not adjudged by any of the Central Excise Officer immediately before the date of grant of acceptance by the Chief Commissioner of Central Excise, Large Taxpayer Unit, shall be deemed to have been issued by Central Excise Officers of the said Unit.
 - (6) Provisions of these rules, in so far as they are not inconsistent with the provisions of this rule shall mutatis mutandis apply in case of a large taxpayer.
3. Notification No. 20/2006 CE (NT) dated 30.09.2006 has notified the following persons to be eligible to opt as large taxpayer:

- (i) Any person engaged in the manufacture or production of goods, except the goods falling under chapter 24 or Pan Masala falling under chapter 21 of the First schedule of the Central Excise Tariff Act, 1985, or
- (ii) a provider of taxable service,

who has paid during the financial year 2004-05 or during the financial year preceding the year of filing of application for large tax payer-

- (a) duties of excise of more than Rs.500 lakhs in cash or through account current; or
- (b) service tax of more than Rs.500 lakhs in cash or through account current; or
- (c) advance tax of more than Rs.1000 lakhs, under the Income Tax Act, 1961,

and is presently assessed to income tax or corporate tax under the Income Tax Act, 1961, under the jurisdiction of Chief Commissioner of Income Tax – I, Bangalore (other than revenue district of Tumkur) and Chief Commissioner of Income Tax – II, Bangalore (other than district of Kolar).

Further, following procedures have also been notified which are to be followed to be eligible to opt as large tax payer:

A large taxpayer who satisfies the conditions mentioned above may file an application in the prescribed form duly completed in all respects to the Chief Commissioner of Central Excise, Large Taxpayer Unit for the city where the large taxpayer is presently assessed to income tax or corporate tax indicating his willingness to be a large taxpayer.

A person willing to operate as large taxpayer shall furnish details of each of the premises already registered under the Central Excise Act, 1944 including the premises of first and second stage dealers and each of the premises registered under Chapter V of the Finance Act, 1994 including the premises of input service distributor.

The Chief Commissioner of Central Excise, Large Taxpayer Unit may after due verification of the application form, grant the acceptance in writing. The process of acceptance would not normally take more than 7 days.

Existing registrations under the Central Excise Act, 1944 or Chapter V of the Finance Act, 1994 shall continue. However, in case a new factory or service provider, input service distributor or first or second stage dealer which becomes liable to be registered, after opting as large taxpayer,

the application for such new registration shall be made before the Chief Commissioner of Central Excise, Large Taxpayer Unit.

4. Notification No.23/2006 CE (N.T.) dated 12.10.2006 has notified revised formats of ER-1 and ER-3 returns under rule 12 of the Central Excise Rules, 2002 and rule 9(7) of CENVAT Credit Rules, 2004. The notification has come into force from 01.11.2006. The revision of the formats of ER-1 and ER-3 has been necessitated following the setting up of the first Large Taxpayer Unit (LTU) in Bangalore. However, the revised ER 1 return form is applicable for all assessees (large taxpayers and others), although the additional details to be provided by a large taxpayer, have been separately indicated.

B. CUSTOMS

(i) Amendments by the Taxation Laws (Amendment) Act, 2006

The Taxation Laws (Amendment) Bill, 2006 was enacted on 13.07.2006, the date on which it received the assent of the President. It has made certain amendments in the Customs Tariff Act, 1975 and the Customs Act, 1962 with the object of rationalizing and simplifying procedures, widening of tax base and plugging loopholes leading to leakage of revenue.

All the amendments made by the Taxation Laws (Amendment) Act, 2006 have come into effect from 13.07.2006.

Amendments in the Customs Act, 1962

1. Speaking order to be issued within 15 days of assessment in case of contrary claims by the assessee [Section 17]

Section 17 of the Customs Act, 1962 governs the provisions in respect of assessment. A new sub-section (5) has been inserted after sub-section (4) in section 17. The new sub-section (5) lays down that where any assessment done under sub-section (2) is contrary to the claim of the importer or exporter regarding valuation of goods, classification, exemption or concessions of duty availed consequent to any notification and in cases other than those where the importer or the exporter, as the case may be, confirms his acceptance of the said assessment in writing, the proper officer shall pass a speaking order within 15 days from the date of assessment of the bill of entry or the shipping bill, as the case may be.

2. Interest to be paid on the duty difference between the provisional and final assessment [Section 18]

Section 18 of the Customs Act lays down the provisions in respect of provisional assessment. Duty is paid in two stages in case of provisional assessment; firstly, at the time of provisional assessment and another at the stage of finalization of assessment. A new sub-section (3) has been inserted in section 18 to levy interest on the duty difference in the provisional and final assessment of duty. This may expedite the recovery of duty short-levied under provisional assessment of duty. Provisions of sub-section (3) are detailed under:

- (1) Sub-section (3) provides that the importer or exporter shall be liable to pay interest, on any amount payable to the Central Government, consequent to the final assessment order.
- (2) The interest shall be payable at the rate fixed by the Central Government under section 28AB.
- (3) This interest shall be payable from the first day of the month in which the duty is provisionally assessed till the date of payment thereof.
- (4) If the refund arising out of the final assessment of goods cleared for home consumption or exportation (in case the amount paid at the time of provisional assessment exceeds the amount determined to be payable at the final assessment) is not refunded within 3 months from the date of final assessment of duty, interest shall be paid to the assessee on such unrefunded amount till the date of refund of such amount.

- (5) This interest shall be payable at the rate fixed by the Central Government under section 27A. The refund of duty and interest thereon shall be subject to the conditions mentioned in point no.6 below.
- (6) The amount of such refundable duty and such interest, if any shall be paid to the importer or the exporter, as the case may be, only if such amount is relatable to:
 - (a) the duty and interest, if any, paid on such duty paid by the importer, or the exporter, as the case may be, if he had not passed on the incidence of such duty and interest, if any, paid on such duty to any other person;
 - (b) the duty and interest, if any, paid on such duty on imports made by an individual for his personal use;
 - (c) the duty and interest, if any, paid on such duty borne by the buyer, if he had not passed on the incidence of such duty and interest, if any, paid on such duty to any other person;
 - (d) the export duty as specified in section 26;
 - (e) drawback of duty payable under sections 74 and 75.

In all other cases the amount of such refund and interest shall be credited to the Consumer Welfare Fund.

3. Adjudication proceedings to conclude in respect of a person who voluntarily deposits the full duty demanded along with interest and penalty equal to 25% of the duty [Section 28(1A)]
 - (i) Section 28(1) provides that where any duty is not/short levied or erroneously refunded or where any interest payable is not/part paid or erroneously refunded, the proper officer may serve notice on the person chargeable with such duty or interest in the case of any import made by any individual for his personal use or by Government or by any educational, research or charitable institution or hospital, within one year from the relevant date. In any other case the notice can be issued within 6 months from the relevant date. However, this period of 1 year and 6 months is extended to 5 years when such short/non levy or non charging or short payment of interest or erroneous refund of duty and interest is by reason of fraud, collusion, or any wilful mis-statement or suppression of facts by the importer or the exporter or the agent or employee of the importer or exporter.
 - (ii) A new sub-section (1A) has been inserted after sub-section (1) in section 28. The new sub-section provides an option to the importer or the exporter or the agent or employee of the importer or exporter to whom a notice has been served by the proper officer for short/non levy or non charging or short payment of interest or erroneous refund of duty and interest by reason of fraud, collusion, or any wilful mis-statement or suppression of facts.
 - (iii) Such a person may pay the duty in full or in part as may be accepted by him including the interest payable thereon under section 28AB and penalty equal to 25% of the duty specified in the notice or the duty so accepted by such person within 30 days of the receipt of the notice.
 - (iv) Further, a proviso has been inserted in sub-section (2) of section 28. Sub-section (2) provides that the proper officer shall consider the representation, if any, made by the person on whom a notice under sub-section (1) is served. He shall determine the amount of duty or interest due from such person and thereupon such person shall pay the amount so determined. However, such amount shall not exceed the amount specified in the notice.
 - (v) The newly inserted proviso lays down that where such a person has paid the duty in full together with interest and penalty, the proceedings in respect of such person and other persons to whom notices (referred to in point 1) have been served shall be deemed to have been concluded in respect of the matters stated therein. The proceedings shall conclude notwithstanding anything contained in sections 135, 135A and 140.

(vi) Another proviso has been inserted in sub-section (2). This proviso lays down that in cases where such person has paid duty in part along with interest and penalty, the proper officer shall determine the amount of duty or interest which will not exceed the amount partly due from such person.

4. Persons furnishing false declaration/documents under section 132, obstructing customs officers under section 133, making preparatory actions for illegal export under section 135A and customs officers guilty of offence under section 136 may also be arrested [Section 104]

Section 104 of the Customs Act grants the power of arrest to officer of customs. Sub-section (1) of section 104 has been substituted by a new sub-section. The new sub-section lays down that if an officer of customs empowered in this behalf by general or special order of the Commissioner of Customs has reason to believe that any person in India or within the Indian customs waters has committed an offence punishable under section 132 or section 133 or section 135 or section 135A or section 136, he may arrest such person and shall, as soon as may be, inform him of the grounds for such arrest. Thus, arrest can also be made in the cases of furnishing false declaration/documents, obstructing customs officers in exercising their powers and making preparation to export any goods in contravention of the provisions of the Customs Act. Further, any officer of customs permitting or doing or abstaining from doing or concealing or conniving at any act or thing whereby any fraudulent export is effected or any duty of customs leviable on any goods is or may be evaded can also be arrested.

5. Summons to be issued in case of any inquiry [Section 108]

Section 108 of the Customs Act empowers any gazetted officer to summon any person to give evidence and to produce documents in any inquiry which such officer is making in connection with the smuggling of any goods. Sub-section (1) of section 108 has been substituted by a new sub-section. The new sub-section lays down that any gazetted officer of customs duly empowered by the Central Government in this behalf, shall have power to summon any person whose attendance he considers necessary either to give evidence or to produce a document or any other thing in any inquiry which such officer is making under this Act. Thus, with this amendment, summons cannot only be issued in connection with smuggling, but for any inquiry under the Customs Act. Further, the gazetted officer issuing the summons should be duly empowered to do so by the Central Government.

6. Use of false and incorrect material to be penalized [New section 114AA]

After section 114A of the Customs Act, section 114AA has been inserted. The new section lays down that if a person knowingly or intentionally

- makes,
- signs or uses, or
- causes to be made,
- signed or used,

any declaration, statement or document which is false or incorrect in any material particular, in the transaction of any business for the purposes of the Customs Act, shall be liable to a penalty. The penalty shall not exceed 5 times the value of goods.

7. Show cause notice before confiscation of goods to be issued only with the prior approval of the officer of customs not below the rank of a Deputy Commissioner of Customs [Section 124]

As per section 124 a written notice is to be issued to the owner of the goods before confiscating any goods or imposing any penalty on such person. Section 124 has been amended to the effect that now such a notice can be issued only with the prior approval of the officer of customs not below the rank of a Deputy Commissioner of Customs.

8. Commissioner to direct any officer of customs subordinate to him to apply to the Commissioner (Appeals) [Section 129D(2)]

Section 129D(2) of the Customs Act gives powers to Commissioner of Customs to pass certain orders. The Commissioner of Customs may of its own motion, call for and examine the record of any proceeding in which an adjudicating authority subordinate to him has passed any order so as to satisfy itself upon the legality or propriety of the order. Thereafter, the Commissioner may direct such authority to apply to the Commissioner (Appeals) to determine such points as may be specified by it.

The Taxation Laws (Amendment) Act, 2006 has amended section 129D(2) to the effect that now the Commissioner may also direct any officer of customs subordinate to him (apart from the adjudicating authority subordinate to him which has passed the order) to apply to the Commissioner (Appeals) to determine such points as may be specified by it.

9. Term of imprisonment increased from 6 months to 2 years in case of furnishing of false declarations/documents etc. [Section 132]

Section 132 of the Customs Act provides for an imprisonment of 6 months or fine, or both, in case of furnishing of false declaration or documents. This term of imprisonment has been increased from 6 months to 2 years.

10. Term of imprisonment increased from 6 months to 2 years in case of obstruction of officers of customs [Section 133]

Section 133 of the Customs Act provides for an imprisonment of 6 months or fine, or both, in case of obstructing officers of customs in exercising their powers. This term of imprisonment has been increased from 6 months to 2 years.

11. Prior sanction of Commissioner of Customs necessary to take cognizance in case of offence under section 135A also [Section 137]

Section 137 lays down that previous sanction of the Commissioner of Customs is necessary for any Court to take cognizance in case of offences under section 132, section 133, section 134 or section 135. Section 137 has been amended to include offences under section 135A i.e., making preparatory actions for illegal export etc. amongst the list of offences for which the cognizance can be taken by the Courts only with the prior sanction of the Commissioner of Customs.

12. Property may be attached provisionally to protect revenue in certain cases [New section 28BA]

A new section 28BA has been inserted by the Taxation Laws (Amendment) Act, 2006. The provisions of this section are:

- (1) During the pendency of any proceeding under section 28 or section 28B, the proper officer may provisionally attach any property belonging to the person on whom notice is served under sub-section (1) of section 28 or sub-section (2) of section 28B, as the case may be, in accordance with the rules made in this behalf under section 142 of the Customs Act, 1962.
- (2) Such an attachment shall be done only when the proper officer is of the opinion that the attachment is necessary for the purpose of protecting the interests of revenue. However, a previous approval of the Commissioner of Customs, by order in writing, is a prerequisite for such provisional attachment.
- (3) Such an attachment can be done for a period of 6 months. This period will commence from the date of the order of the Commissioner of Customs permitting such provisional attachment.
- (4) However, this period may be extended by the Chief Commissioner of Customs by such further period or periods as he thinks fit. The reasons for such an extension shall be recorded in writing. It is to be noted that the total period of extension in any case shall not exceed 2 years.

- (5) If an application for settlement of a case under section 127B is made to the Settlement Commission, the period commencing from the date on which such an application is made and ending with the date on which an order under section 127C(1) is made shall be excluded from the extended period mentioned in point (4).

13. Seized goods, documents and things pending adjudication to be released provisionally [New section 110A]

A new section 110A has been inserted after section 110 of the Customs Act. The new section lays down that any goods, documents or things seized under section 110, may, pending the order of the adjudicating officer, be released to the owner. Such release shall be made when the owner executes a bond in the proper form with such security and conditions as the Commissioner of Customs may require.

14. Information in respect of persons in certain cases to be published [New section 154B]

This new section, added by the Taxation Laws (Amendment) Act, 2006 provides for publishing the name of any person and particulars of any proceedings in relation to such person, in public interest. The provisions are discussed below in detail:

- (1) The Central Government may publish name of any person and any other particulars relating to any proceedings in respect of such person if it is of the opinion that it is necessary or expedient in the public interest to do so. The Government can do the publication in such manner as it thinks fit.
- (2) The publication shall be made in relation to any penalty only after the time for presenting an appeal to the Commissioner (Appeals) or the Appellate Tribunal expires without an appeal being presented or the appeal, if presented, gets disposed of.
- (3) In the case of a firm, company or other association of persons, the names of the partners of the firm, directors, managing agents, secretaries and treasurers or managers of the company, or the members of the association, as the case may be, may also be published if, in the opinion of the Central Government, circumstances of the case justify it.

Amendment in the Customs Tariff Act, 1975

1. The words “all such countries” clarified to mean “developing countries each with less than 3% import share” in proviso to section 8B(1)

As per the proviso to section 8B(1) of the Customs Tariff Act, 1975 articles originating from developing country are exempt from safeguard duty so long as the share of imports of that article from that country does not exceed 3% of the total imports of that article into India. In case of articles originating from more than one developing country, the exemption will be available if the aggregate of imports from all such countries taken together does not exceed 9% of the total imports of that article into India.

In the said proviso the words “all such countries” have been substituted with the words “developing countries each with less than 3% import share”. Thus, it has been clarified that in case of articles originating from more than one developing country the exemption from safeguard duty shall be available only if the aggregate of import from all developing countries each with less than 3% import share does not exceed 9% of the total imports of that article into India.

(ii) Significant amendments made through Notifications/Circulars issued between 01.05.2006 and 30.04.2007

1. Notification No.80/2006-Cus (N.T.) dated 13.07.2006 has amended the Customs and Central Excise Duties Drawback Rules, 1995. These rules have been rechristened as Customs, Central Excise Duties and Service Tax Drawback Rules, 2006 and have been accordingly amended to provide for the drawback of service tax paid on taxable services used as input services in the manufacture or processing of export goods.

The new drawback rates shall now also take into account the incidence of service tax paid on taxable services which are used as input services in the manufacturing or processing of

export goods. The exporters should not avail of the refund of this tax through any other mechanism while claiming the all industry rate of drawback.

C. SERVICE TAX

- (i) Significant amendments made through Notifications/Circulars issued between 01.05.2006 and 30.04.2007

Exemptions

1. Notification No. 7/2006 ST dated 01.03.2006 exempting taxable services, provided or to be provided to any person, by Reserve Bank of India, from the whole of service tax leviable thereon has been superseded by Notification No. 22/2006 ST dated 31.05.2006. This notification exempts the following taxable services from the whole of the service tax leviable thereon:
 - (i) taxable services provided or to be provided to any person, by the Reserve Bank of India;
 - (ii) taxable services provided or to be provided by any person, to the Reserve Bank of India when the service tax for such services is liable to be paid by the Reserve Bank of India under sub-section (2) of section 68 of the said Finance Act read with rule 2 of the Service Tax Rules, 1994;
 - (iii) taxable services received in India from outside India by the Reserve Bank of India under section 66A of the Finance Act, 1994.
2. Following amendments have been made in Notification No. 1/2006 ST dated 01.03.2006 which grants partial exemptions from service tax to certain specified services:
 - (i) Abatement granted to erection, commissioning or installation service under a contract for supplying a plant, machinery or equipment and erection, commissioning or installation thereof has been extended to structures as well. This amendment is in view of the modification made in the definition of erection, commissioning or installation service by the Finance Act, 2006 [Notification No. 21/2006 ST dated 23.05.2006].
 - (ii) Business auxiliary service, in relation to production or processing of parts and accessories used in the manufacture of cycles, cycle rickshaws and hand-operated sewing machines, for, or on behalf of, the client has been granted an abatement of 30% from the gross amount charged for such service. This abatement is available when the gross amount charged from the client is inclusive of the cost of inputs and input services, whether or not supplied by the client.
 However, the exemption is not available in cases where –
 - (i) the CENVAT credit of duty paid on inputs or capital goods or the CENVAT credit of service tax on input services, used for providing such taxable service has been taken under the provisions of the CENVAT Credit Rules, 2004; or
 - (ii) the service provider has availed the benefit under Notification No. 12/2003-ST, dated 20.06.2003 [Notification No. 23/2006 ST dated 02.06.2006].
3. Notification No. 25/2006 ST dated 13.07.2006 has exempted the taxable services provided or to be provided by a practising chartered accountant, a practising cost accountant and a practising company secretary, in their professional capacity, to a client, relating to representing the client before any statutory authority in the course of proceedings initiated under any law for the time being in force, by way of issue of notice, from the whole of service tax leviable thereon.
4. Notification No. 31/2006 ST dated 11.12.2006 has exempted the taxable service provided by an insurer, carrying on general insurance business, to a policy holder for the insurance of sheep, from the whole of service tax leviable thereon. However, the exemption contained in this notification shall be valid only upto 31.12.2009.
5. Notification No. 4/2007 ST dated 01.03.2007 has amended Notification No.6/2005 ST dated 01.03.2005 in order to raise the exemption limit in case of small service providers from the current Rs.4,00,000 to Rs.8,00,000 with effect from 01.04.2007. Thus, taxable services of aggregate value not exceeding Rs.8,00,000 in any financial year would be exempt from service tax if the

aggregate value of taxable services rendered by a provider of taxable service from one or more premises does not exceed Rs.8,00,000 in the preceding financial year.

6. Consequent upon the increase in the threshold exemption limit from Rs.4 lakh to Rs.8 lakh, the limit for obtaining service tax registration has also been increased from Rs.3 lakh to Rs.7 lakh by amending Notification Nos. 26/2005-ST and No.27/2005-ST, both dated 07.06.05 vide Notification Nos. 5, 6 & 7/2007 ST dated 01.03.07. This amendment is effective from 01.04.2007.
7. Notification No. 8/2007 ST dated 01.03.2007 has exempted the taxable services provided or to be provided by a resident welfare association under section 65(105)(zzze) to its members from whole of the service tax leviable thereon. However, the exemption is subject to the condition that the total consideration received from an individual member by the said association for providing the said services does not exceed Rs.3,000 per month. This service would otherwise be taxable under the category of membership of clubs or association.

It has been clarified vide F.No.137/68/2007-CX.4 dated 08.05.2007 that a resident welfare association registered as a co-operative society with Registrar of Co-operative Societies is eligible to avail exemption from levy of service tax vide Notification No.8/2007 ST dated 01.03.2007 provided the following conditions are satisfied, namely:-

- (i) The exemption is available for the services specified under section 65(105)(zzze) of the Finance Act, 1994 and provided or to be provided by the association to its members.
 - (ii) The sole criterion for membership of the resident welfare association is the residential status of a person in a residential complex or locality i.e., membership of the association is restricted only to the residents of the complex or locality.
 - (iii) The value of total consideration received from an individual member by the association for providing the services should not exceed Rs.3,000/- per month.
8. With effect from 01.04.2007, Notification No. 9/2007 ST dated 01.03.2007 exempts all taxable services provided or to be provided by Technology Business Incubators (TBI)/Science and Technology Entrepreneurship Parks (STEP) recognized by National Science and Technology Entrepreneurship Board (NSTEDB) of the Department of Science & Technology from the whole of service tax leviable thereon. The exemption contained in this notification shall be subject to the following conditions:
 - (i) the STEP or the TBI, who intends to avail the exemption, shall furnish the requisite information containing the details of the incubator along with the information received from each incubatee to the concerned Assistant/Deputy Commissioner of Central Excise before availing the exemption; and
 - (ii) the STEP or the TBI shall thereafter furnish the information in the formats mentioned above in the same manner before the 30th day of June of each financial year.
 9. With effect from 01.04.2007, Notification No. 10/2007 ST dated 01.03.2007 has exempted taxable services provided or to be provided by an (incubatee) entrepreneur located within the premises of a TBI/STEP recognized by the NSTEDB of the Department of Science and Technology Government of India from the whole of the service tax leviable thereon subject to the following conditions:-
 - (i) the entrepreneur enters into an agreement with the TBI or the STEP as an incubatee, to enable himself to develop and produce hi-tech and innovative products; and
 - (ii) the total business turnover of such entrepreneur does not exceed Rs.50 lakh during the previous financial year.

Further, the exemption contained in this notification shall apply for a period of 3 years from the date on which such entrepreneur enters into an agreement with the TBI or the STEP.

The exemption for taxable services under this notification shall not be available for any taxable services provided or to be provided immediately after the total business turnover of the entrepreneur exceeds Rs.50 lakh during a given financial year.

10. Notification No. 11/2007 ST dated 01.03.2007 has exempted the technical testing and analysis services of new drugs, including vaccines and herbal remedies, on human participants so as to ascertain the safety and efficacy of such drugs by a Clinical Research Organization (CRO) (approved to conduct clinical trials by the Drugs Controller General of India) from the whole of service tax leviable thereon.
11. Notification No. 12/2007 ST dated 01.03.2007 has exempted the taxable services, provided or to be provided, under an agreement, by any person to other person who has the right to authorise any person to exhibit cinematograph film, from the whole of the service tax leviable thereon subject to the following conditions:
 - (i) that the service provided or to be provided is in relation to the delivery of the content of the cinematograph film; and
 - (ii) that the content of such film, being in digitized form, after its encryption, is transmitted directly to a cinema theatre for exhibition through the use of satellite, microwave or terrestrial communication line and not by any physical means including CD and DVD.

Explanation. – For the purposes of this notification, -

- (a) “cinematograph film” means a film certified under section 5A of the Cinematograph Act, 1952;
 - (b) “cinema theatre” means a place which is licenced under Part III of the Cinematograph Act, 1952, or under any other law for the time being in force in a state for the exhibition of a cinematograph film.
12. During the period between 01.04.2000 and 04.02.2004 there was a practice of not levying service tax on services provided by a tour operator providing services in relation to transport of passengers (other than services provided in relation to package tour) operating under a contract carriage permit issued by the appropriate transport authority. However, such services were liable to service tax under section 65(105)(n) of the Finance Act.

Therefore, in exercise of the powers conferred by section 11C of the Central Excise Act 1944 read with section 83 of the Finance Act, the Central Government has directed vide Notification No.15/2007 ST dated 04.04.2007 that service tax on 60% of the gross amount charged by such tour operators shall not be required to be paid in respect of such taxable service on which the service tax was not being levied during the aforesaid period in accordance with the said practice.

Other Amendments

13. When Service Tax (Determination of Value) Rules, 2006 were notified on 19.04.2006, Rule 6(2)(iii) inter alia provided that the rail fare collected by “air travel agent” in respect of service provided by him does not form part of the taxable service. This error has now been rectified vide Notification No. 24/2006 ST dated 27.06.2006 which has substituted the words “air travel agent” with the words “rail travel agent”.
14. Following amendments have been made in the Service Tax Rules, 1994 vide
 - (i) In rule 2, after sub-rule (ccc), sub-rule (cccc) has been inserted which defines “large taxpayer” to have the meaning assigned to it in the Central Excise Rules, 2002. This has been done to incorporate the concept of large taxpayer in the service tax provisions [Notification No. 28/2006 ST dated 30.09.2006]
 - (ii) With effect from 01.04.2004, rule 2(1)(d)(vii) has been amended to the effect that service tax is required to be paid under reverse charge method, i.e., where service tax is to be paid by service receiver, in relation to sponsorship service only if the recipient of service is located in India. Therefore, if the recipient of sponsorship service is located outside India, service tax would be required to be paid by the service provider and not by the recipient [Notification No. 1/2007 ST dated 01.03.2007]

Accordingly, similar amendment has also been made in Notification No. 36/2004 ST dated 31.12.2004 vide Notification No. 3/2007 ST dated 01.03.2007.

- (iii) Sub-rule (2) of rule 4 has been substituted by a new sub-rule vide Notification No.29/2006 ST dated 02.11.2006. The new sub-rule (2) provides that where a person, liable for paying service tax on a taxable service:

- (i) provides such service from more than one premises or offices; or
- (ii) receives such service in more than one premises or offices; or
- (iii) is having more than one premises or offices, which are engaged in relation to such service in any other manner, making such person liable for paying service tax,

and has centralised billing system or centralised accounting system in respect of such service, and such centralised billing or centralised accounting systems are located in one or more premises, he may, at his option, register such premises or offices from where centralised billing or centralised accounting systems are located.

Prior to this amendment, only the person providing taxable service from more than one premises and having centralized billing or accounting in respect of such service could take centralized registration of premises from which such centralized billing was done or where such centralized accounting system was maintained. However, with this amendment the service receiver or any other person made liable to pay service tax, having centralized accounting/billing for such service will be eligible to take centralized registration.

- (iv) Sub-rule (3) of rule 4 has been substituted by a new sub-rule vide Notification No.29/2006 ST dated 02.11.2006. The new sub-rule (3) provides that in all cases where tax payer opts for centralised registration, including those who have applied for such registration but have not been granted such centralised registration, the registration shall be granted by the Commissioner of Central Excise having jurisdiction over the premises for which centralized registration is sought (i.e., the premises from where centralized billing or accounting is done).

However, such provisions shall not be applicable to the registration granted to the premises or offices having such centralised billing or centralised accounting systems, prior to the 2nd day of November, 2006.

Prior to this amendment, centralized registrations were granted by the Commissioner or the Chief Commissioner of Central Excise or DGST, as the case may be, depending on the location of premises where centralized billing or accounting system was maintained as well as from where the taxable service was provided.

- (v) Following amendments have been made by amending sub-rule (5) of rule 4 and Form ST-1 and ST-2:
- (i) While intimating any change in the information furnished at the time of obtaining registration certificate, the assessee would be required to submit only a self-certified copy of the registration certificate instead of original registration certificate.
 - (ii) Department shall issue the amended registration certificate after cancelling the original registration certificate issued earlier [Notification No. 1/2007 ST dated 01.03.2007].
- (vi) Sub-rule (4) of rule 5 lays down that every assessee shall make available the prescribed records at the registered premises for inspection and examination by the Central Excise Officer. This sub-rule has been amended vide Notification No.29/2006 ST dated 02.11.2006 to the effect that now the audit party deputed by the Comptroller and Auditor General of India can also inspect and examine the records and the assessee shall make available such records to them.
- (vii) With effect from 01.10.2006, Notification No. 27/2006-ST dated 21.09.2006 has made it compulsory for the assessee, who has paid service tax of Rs.50,00,000 or above in the preceding financial year or has already paid service tax of Rs.50,00,000 in the current financial year, to deposit the service tax liable to be paid by him electronically, through internet banking. This has been done by amending sub-rule (2) of rule 6.

Circular No. 88/06/2006 ST dated 06.11.2006 has clarified the following regarding the interpretation of qualifying amount of service tax of such Rs.50 lakh paid by the assessee:

- (i) For a person providing taxable service from more than one premises, where each such premises is separately registered with the department for payment of service tax, the criterion of Rs.50 lakh would apply to each registered premises individually, as each registered premises is separately an assessee in terms of law. Similar is the situation in the case of a person paying service tax on taxable service received by him.

However, in case of a Large Taxpayer (LTU), the cumulative service tax paid by all registered premises of such Large Taxpayer will be taken into account for satisfaction of criterion of payment of service tax amount of Rs 50 lakh.

- (ii) If a person pays service tax from a registered premises for both the taxable services provided by him and the taxable service received by him on which he is liable to pay service tax, the cumulative service tax paid, i.e., service tax paid on taxable service provided from and service tax paid on taxable service received in such registered premises would be taken into account for the purposes of satisfaction of criterion of payment of service tax amount of Rs.50 lakh.
- (iii) Further, for the purposes of calculation of this amount of Rs.50 lakh the total service tax paid by cash plus CENVAT credit would be taken into account as service tax paid amount. Therefore, if an assessee has paid service tax of Rs.50 lakh (in preceding financial year or the current year) in cash plus CENVAT credit, such assessee, if he pays any further service tax in cash, would be required to make mandatory e-payment.
- (viii) Sub-rule (4A) of rule 6 has been substituted and sub-rule 4B inserted to provide for self-adjustment of excess service tax paid, subject to specified conditions. So far, self-adjustment of excess service tax paid was available only to the assessee who opted for centralised registration. Further, the adjustment was allowed only on account of delayed receipt of details of payment from the branch offices.

With effect from 01.03.2007, self-adjustment of excess service tax paid has been extended to all the assessee. However, such an adjustment would be subject to the following conditions:

- (i) Self-adjustment of excess credit would not be allowed in case of reasons involving interpretation of law, taxability, classification, valuation or applicability of any exemption notification.
- (ii) Excess amount paid and proposed to be adjusted should not exceed Rs.50,000 for the relevant month or quarter. However, in case of assessee opting for centralized registration excess amount can be adjusted without any monetary limit provided the excess amount paid is on account of delayed receipt of details of payments from branch offices.
- (iii) Adjustment can be made only in the succeeding month or quarter.
- (iv) The details of self-adjustment should be intimated to the Superintendent of Central Excise within a period of 15 days from the date of such adjustment [Notification No. 1/2007 ST dated 01.03.2007].
- (ix) Rule 7B has been inserted vide Notification No. 1/2007 ST dated 01.03.2007 to allow an assessee to submit a revised return, in Form ST-3, in triplicate, to correct a mistake or omission, within a period of 60 days from the date of submission of the return under rule 7. It has been clarified that where an assessee submits a revised return, the 'relevant date' for the purpose of recovery of service tax, if any, under section 73 of the Act shall be the date of submission of such revised return.
- (x) Rule 10 has been inserted after Rule 9 which lays down the procedure and facilities for the large taxpayer. This has been done to incorporate the concept of large taxpayer in the service tax provisions.

The provisions of this rule are discussed below:

Notwithstanding anything contained in these rules, the following shall apply to a large taxpayer,-

- (1) A large taxpayer shall submit the returns, as prescribed under these rules, for each of the registered premises. A large taxpayer who has obtained a centralized registration under rule 4(2) shall submit a consolidated return for all such premises.
- (2) A large taxpayer, on demand, may be required to make available the financial, stores and CENVAT credit records in electronic media, such as, compact disc or tape for the purposes of carrying out any scrutiny and verification, as may be necessary.
- (3) A large taxpayer may, with intimation of at least 30 days in advance, opt out to be a large taxpayer from the first day of the following financial year.
- (4) Any notice issued but not adjudged by any of the Central Excise Officer administering the Act or rules made thereunder immediately before the date of grant of acceptance by the Chief Commissioner of Central Excise, Large Taxpayer Unit, shall be deemed to have been issued by Central Excise Officers of the said unit.
- (5) Provisions of these rules, in so far as they are not inconsistent with the provisions of this rule shall mutatis mutandis apply in case of a large taxpayer [Notification No. 28/2006 ST dated 30.09.2006].

15. As per sub-rule (2) of rule 3 of Export of Services Rules, 2005 any taxable service shall be treated as exported only when the following conditions are satisfied:-

- (a) such service is delivered outside India and used outside India; and
- (b) payment for such service provided outside India is received by the service provider in convertible foreign exchange.

This sub-rule has been substituted by the following sub-rule vide Notification No. 2/2007 ST dated 01.03.2007:

The provision of any taxable service specified in sub-rule (1) shall be treated as export of service when the following conditions are satisfied:-

- (a) such service is provided from India and used outside India; and
- (b) payment for such service provided outside India is received by the service provider in convertible foreign exchange.

Thus, following amendments have been made in rule 3(2):

- (i) The words 'delivered outside India and used outside India' have been substituted with the words 'provided from India and used outside India'.
- (ii) It has been clarified that both rule 3(1) and rule 3(2) have to be satisfied for provision of service to be treated as export of service.

The explanation remains unchanged.

16. Circular No. 83/1/2006 ST dated 04.07.2006 has clarified that services such as transfer of money through money orders, operation of savings accounts, issue of postal orders provided by the Department of Posts are not liable to service tax under banking and other financial services. Banking and other financial services are defined under section 65(12). Such services provided to a customer by a banking company or a financial institution including a non-banking financial company or any other body corporate or any other person to a customer are liable to service tax under section 65(105)(zm). The expression 'any other person' appearing in section 65(105)(zm) is to be read ejusdem generis with the preceding words. The expression 'other financial services' appearing under section 65(12)(a)(ix) is a residuary entry and includes those services which are normally rendered by banks or financial institutions.

Hence, banking and other financial services provided by a banking company or a financial institution or a non-banking financial company or any other service provider similar to a bank or a

financial institution are liable to service tax under section 65(105)(zm) of the Finance Act, 1994. Department of Posts is not similar to a bank or a financial institution and hence does not fall within the category of any other similar service provider.

Note: The Finance Act, 2007 has substituted the words "or any other person" in the definition of banking and other financial services provided under section 65(12) with the words "or commercial concern". This amendment has come into effect from 11.05.2007.

17. Circular No. 84/2/2006 ST dated 19.09.2006 has clarified that any club or association that enjoys exemption under the provisions of Income Tax Act on the ground of being a public charitable institution does not automatically get excluded from levy of service tax under section 65(105)(zzze) read with section 65(25a) of the Finance Act, 1994 as exemption under the Income Tax Act on the ground of being a public charitable institution is of no consequence to levy of service tax. Levy of service tax is entirely governed by the provisions contained in the Finance Act, 1994 and the rules made thereunder.
18. Circular No. 85/3/2006 ST dated 17.10.2006 has clarified following issues in respect of levy of service tax on international journey by aircraft:

Sl.No.	Issue	Clarification
1	In the case of international journey commencing from an Indian airport involving stopover/transfer at intermediate airports outside India before reaching the destination (say Mumbai-Dubai-London-New York), whether service tax would be leviable on the value indicated in the ticket or on the value attributable to the first sector (Mumbai-Dubai)?	International journey is from Mumbai to New York. Stopover/transfer at intermediate airports is incidental or part of the main journey. Stop over/transfer at intermediate airports outside India is of no relevance or consequence for levy of service tax under section 65(105)(zzzo) read with section 66 of the Finance Act, 1994. Service tax is leviable on the total value of the ticket representing the consideration of a single composite service.
2.	In case the international journey also includes travel in a domestic sector as part of the international journey (say Delhi-Mumbai-London), whether service tax is leviable excluding the value attributable to the domestic sector or on the total value of the ticket treating the domestic sector as integral part of international journey?	Service tax is leviable on the total value of the ticket.
3.	In the case of round trip/return ticket, whether service tax is leviable on the total value of the ticket or only on half the value of the ticket?	Service tax is leviable on the total value of the ticket.
4.	In the case of journey commencing from an airport outside India and completed at an airport outside India but including a sector wherein the passenger disembarks and subsequently embarks at an Indian airport as part of international journey (say Sydney-Mumbai-Dubai-Singapore-Sydney), whether service tax is leviable for Mumbai-Dubai sector only or on the total value of	Service tax is not leviable in such cases.

	the ticket?	
5.	Whether ticket issued outside India for an international journey commencing from India (say Delhi–London) is leviable to service tax?	Service tax is payable by the service provider for the taxable service provided. Place of purchase/issue of ticket is of no relevance or consequence to determine the levy of service tax under section 65(105)(zzzo) read with section 66 of the Finance Act, 1994.

19. Circular No. 86/4/2006 ST dated 01.11.2006 has clarified that institutes like IITs or IIMs are not liable to pay service tax prior to 1.5.2006 under the category of “manpower recruitment or supply service”. As regards the period after 1.5.2006, decision should be taken after taking into account all material facts on case to case basis.
20. Circular No. 87/05/2006 ST dated 06.11.2006 has clarified following issues relating to authorized motor vehicle dealers and service stations:

Sl.No.	Issue	Clarification
1.(a)	Whether the mark-up (profit) on the spare parts sold by a service station during the servicing of vehicles is liable to payment of service tax?	As regards, the issue relating to sale of spare parts and consumables, Notification No. 12/2003 ST dated 20.06.2003, exempts service tax to the extent of value of the goods and materials sold by the service provider to the service recipient, if documentary proof of such sale exists and no credit of excise duty paid on such spares or consumables have been taken.
1.(b)	Whether exemption can be claimed on the cost of consumables that get consumed during the course of providing service?	It may, however be pertinent to note that for availing such exemption, the goods must be sold and consequently, they must be available (whether independently or as a part used for repair of a vehicle) for sale. In other words, the exemption would not be available to such consumables which have been consumed during the process of providing service and are not available for sale.
2.	Whether ‘free services’ given by the authorized dealers (for which they are reimbursed by the vehicle manufacturers) are subjected to service tax?	As regards ‘free servicing’ (where the customer does not pay any charges) of the motor vehicles, normally the service charges are reimbursed by the vehicle manufacturers, who promises such a facility to attract customer. As the law does not in any way restricts the levy of service tax only on the service charges received from the recipient of the service, therefore, such reimbursements are subject to service tax.
3.	Whether the commission received by the automobile dealers from Banks/Non Banking Financial Companies (NBFC), for introducing the customers seeking finances/loans to such banks/NBFCs is subjected to service tax?	In some cases, the automobile dealers help the buyers of the vehicles for arranging the finances. For this, they have a tie-up with Banks/Non-banking Finance Companies. The customers are advised by the dealers to approach such financial companies for taking loans. The automobile dealers get commission from such financial companies for directing the customers to the latter. By this activity, the automobile dealers ‘promote or

	Further, in case part of these incentives are passed on by the dealers to the customers, whether tax would be leviable only on that part of incentive, which is retained by the dealers or whether it would be on full amount?	market the services provided by their customer (i.e., the financial institution) and are therefore covered under "taxable business auxiliary service". The tax is payable on the gross commission received by the automobile dealer. In some cases, the dealers share part of their commission with their customers to attract them. However, this is an independent transaction between the automobile dealer and the purchaser of the vehicle and does not involve the service rendered by the automobile dealer to the finance company. Therefore, the tax payable by the dealer would be on the gross amount received from the financial company and not on the balance amount, i.e., after excluding the amount that he passes on to the customer.
4.	Whether service tax is chargeable on the amounts received for servicing/repair of the commercial vehicles?	As regards 'authorized service stations', the taxable service means any service provided or to be provided to a customer by an authorized service station in relation to any service, repair, reconditioning or restoration of motor cars, light motor vehicles or two wheeled motor vehicles, in any manner. Further, a 'light motor vehicle' means any motor vehicle constructed or adapted to carry more than 6 messengers, but not more than 12 passengers, excluding driver. Similarly, as per the 'Motor Vehicle Act', a 'motor car means any motor vehicle other than a transport vehicle, omnibus, road-roller, tractor, motor cycle or invalid carriage'. In other words, servicing, repair, reconditioning or restoration of specified types of vehicles (whether they are used for commercial purposes or not) fall under the category of taxable services. However, servicing of vehicles like trucks is not within the ambit of service tax.

21. Circular No. 89/7/2006 ST dated 18.12.2006 has clarified that service tax shall not be leviable on fee collected by Public Authorities while performing statutory functions/duties under the provisions of a law. However, if such authority performs a service, which is not in the nature of statutory activity and the same is undertaken for a consideration not in the nature of statutory fee/levy, then in such cases, service tax would be leviable, if the activity undertaken falls within the ambit of a taxable service.

A number of sovereign/public authorities (i.e. an agency constituted/set up by government) perform certain functions/duties, which are statutory in nature. These functions are performed in terms of specific responsibility assigned to them under the law in force. For example, the Regional Reference Standards Laboratories (RRSL) undertake verification, approval and calibration of weighing and measuring instruments; the Regional Transport Officer (RTO) issues fitness certificate to the vehicles; the Directorate of Boilers inspects and issues certificate for boilers; or Explosive Department inspects and issues certificate for petroleum storage tank, LPG/CNG tank in terms of provisions of the relevant laws. Fee as prescribed is charged and the same is ultimately deposited into the Government Treasury.

The Circular explains that the activities performed by the sovereign/public authorities under the provision of law are in the nature of statutory obligations which are to be fulfilled in accordance with law. The fee collected by them for performing such activities is in the nature of compulsory levy as per the provisions of the relevant statute, and it is deposited into the Government treasury. Such activity is purely in public interest and it is undertaken as mandatory and statutory function. These are not in the nature of service to any particular individual for any consideration. Therefore, such an activity performed by a sovereign/public authority under the provisions of law does not constitute provision of taxable service to a person and, therefore, no service tax is leviable on such activities.

22. Circular No. 91/2/2007 ST dated 12.03.2007 has been issued regarding levy of service tax on interconnect usage charges (IUC) on interconnection service provided by one telecom operator to another. The interconnection service is provided by one telegraph authority to another to enable the telephone subscribers of these telegraph authorities to connect with each other. Interconnection in technical terms means the commercial and technical arrangements under which service providers connect their equipment, networks, and services to enable their customers to have access to the customers, services, and networks of other service providers. For providing interconnection, the telegraph authority collects interconnect usage charges (IUC).

The Finance Act, 2007 has incorporated a new definition of 'telecommunication service' vide clause (104) of section 65 of the Finance Act, 1994 and IUC has been specifically incorporated in the definition of 'telecommunication service' to make it a taxable service. Further, any service provided or to be provided, to any person, by a telegraph authority in relation to 'telecommunication service' has been made taxable. This amendment has come into effect from 01.06.2007. Therefore, after this amendment comes into effect, service tax would be applicable to IUC charges. It has therefore been clarified that for the period prior to the date when the amended definition of "telecommunication service" comes into effect, service tax is not applicable to IUC.

23. Service tax is leviable on foreign exchange (forex) broking service under the category of 'banking and other financial service'. In terms of the provisions of the Finance Act, 1994, foreign exchange broker includes a money changer (authorized dealer of foreign exchange). Circular No. 92/3/2007 ST dated 12.03.2007 has been issued to answer the question as to whether the service provided by a money changer in relation to exchange of foreign currency is a forex broking service for applicability of service tax levy under 'banking and other financial services'.

It has been noted that 'money changing' and 'foreign exchange broking' are two distinct activities. Money changing is an activity of sale and purchase of foreign exchange at the prevalent market rates. On the other hand, foreign exchange broking is the activity performed as an intermediary, on a commission/brokerage basis, for facilitating the clients who wish to buy or sell foreign exchange. The foreign exchange broker providing foreign exchange broking service does not hold title to the foreign exchange. Accordingly, Board is of the view that service tax is not leviable on money changing per se, as such activity does not fall under the category of foreign exchange broking.

RECENT AMENDMENTS IN DIRECT TAXES AND INDIRECT TAXES

Students are advised to study thoroughly the Supplementary Study Paper-2006 on Direct taxes and Indirect taxes for the Final Course. This contains the amendments made by the Finance Act, 2006 as well as the relevant Notifications/Circulars issued up to 30.04.2006. This Supplementary Study Paper is available at various branch and regional sales counters of the Institute. This is very important since considerable weightage is being given to the latest amendments in the examinations.

Students may note that the Board of Studies has come out with a publication "Select Cases in Direct and Indirect Taxes [2006] – An Essential Reading for Final Course". This contains important recent judgements of Supreme Court, High Court and Appellate Tribunal in both Direct Taxes and Indirect Taxes.



The Institute of Chartered Accountants of India

FINAL (NEW) COURSE

SYLLABUS

GROUP I

- Paper – 1 : Financial Reporting
- Paper – 2 : Strategic Financial Management
- Paper – 3 : Advanced Auditing and Professional Ethics
- Paper – 4 : Corporate and Allied Laws

GROUP II

- Paper – 5 : Advanced Management Accounting
- Paper – 6 : Information Systems Control and Audit
- Paper – 7 : Direct Tax Laws
- Paper – 8 : Indirect Tax Laws

PAPER – 1 : FINANCIAL REPORTING
(One paper – Three hours – 100 marks)

Level of Knowledge: Advanced knowledge

Objectives:

- (a) To gain ability to analyze financial statements including consolidated financial statements of group companies and financial reports of various types of entities,
- (b) To gain ability to apply valuation principles,
- (c) To familiarise with recent developments in the area of financial reporting,
- (d) To gain ability to solve financial reporting and valuation cases.

Contents:

1. Accounting Standards, Accounting Standards Interpretations and Guidance Notes on various accounting aspects issued by the ICAI and their applications.
2. Overview of International Accounting Standards (IAS)/International Financial Reporting Standards (IFRS), Interpretations by International Financial Reporting Interpretation Committee (IFRIC), Significant difference vis-a-vis Indian Accounting Standards.
Understanding of US GAAP,
Applications of IFRS and US GAAP.
3. Corporate Financial Reporting - Issues and problems with special reference to published financial statements.
4. Accounting for Corporate Restructuring (including inter-company holdings).
5. Consolidated Financial Statements of Group Companies Concept of a Group, purposes of consolidated financial statements minority interest, Goodwill, Consolidation procedures – Minority interests, Goodwill, Treatment of pre- acquisition and post-acquisition profit.
Consolidation with two or more subsidiaries, consolidation with foreign subsidiaries.
Consolidated profit and loss account, balance sheet and cash flow statement.
Treatment of investment in associates in consolidated financial statements.
Treatment of investments in joint ventures in consolidated financial statements.
6. Accounting and Reporting of Financial Instruments
Meaning, recognition, derecognition and offset, compound financial instruments
Measurement of financial instruments
Hedge accounting
Disclosures
7. Share based payments
Meaning, Equity settled transactions, Transaction with employees and non- employees
Determination of fair value of equity instruments
Vesting conditions
Modification, cancellation and settlement
Disclosures
8. Financial Reporting by Mutual funds, Non-banking finance companies, Merchant bankers, Stock and commodity market intermediaries.
9. Valuation
(a) Concept of Valuation

- (b) Valuation of Tangible Fixed Assets
- (c) Valuation of Intangibles including Brand Valuation and Valuation of Goodwill
- (d) Valuation of Liabilities
- (e) Valuation of Shares
- (f) Valuation of Business

10. Developments in Financial Reporting

- (a) Value Added Statement
- (b) Economic Value Added, Market Value Added, Shareholders' Value Added
- (c) Human Resource Reporting
- (d) Inflation Accounting

Note: If either old Accounting Standards (ASs), Accounting Standards Interpretations (ASIs), Guidance Notes (GNs), Announcements and Limited Revisions to ASs are withdrawn or new ASs, GNs, Announcements and Limited Revisions to AS are issued by the Institute of Chartered Accountants of India in place of existing ASs, ASIs, GNs, Announcements and Limited Revisions to AS, the syllabus will accordingly include/exclude such new developments in the place of the existing ones with effect from the date to be notified by the Institute.

PAPER – 2 : STRATEGIC FINANCIAL MANAGEMENT

(One paper – Three hours – 100 marks)

Level of Knowledge: Advanced knowledge

Objective:

To apply financial management theories and techniques for strategic decision making.

Contents:

1. Financial Policy and Corporate Strategy
 - Strategic decision making framework
 - Interface of Financial Policy and strategic management
 - Balancing financial goals vis-à-vis sustainable growth.
2. Project Planning and Capital Budgeting
 - Feasibility study
 - Cash flow Projections – Impact of taxation, depreciation, inflation and working capital
 - Capital Budgeting Decisions - Certainty Equivalent approach, Evaluation of Risky Investment Proposals, Risk and Return analysis, Simulation and decision tree analysis, Sensitivity analysis, Capital Rationing, Adjusted Net Present Value, Replacement decisions, Application of Real Options in capital budgeting, Impact of inflation on capital budgeting decisions
 - Preparation of Project Report
 - Social cost benefit analysis.
3. Leasing decision including cross border leasing
4. Dividend Decisions
 - Dividend theories, Determinants of dividend policies.
5. (a) Indian Capital Market including role of various primary and secondary market institutions

(b) Capital Market Instruments

Financial derivatives – stock futures, stock options, index futures, index options

Option valuation techniques : Binomial model, Black Scholes Option Pricing Model, Greeks – Delta, Gamma, Theta, Rho and Vega

Pricing of Futures – Cost of carry model

Imbedded derivatives

(c) Commodity derivatives

(d) OTC derivatives -Swaps, Swaptions, Forward Rate Agreements (FRAs), Caps, Floors and Collors.

6. Security Analysis

Fundamental analysis - Economic analysis, Industry analysis and Company Analysis

Bond valuation, Price Yield relationship, Bond Price forecasting – application of duration and convexity, Yield curve strategies

Technical Analysis – market cycle model and basic trend identification, different types of charting, support and resistance, price patterns, moving averages, Bollinger Bands, momentum analysis.

7. Portfolio Theory and Asset Pricing

Efficient Market Theory – Random walk theory ; Markowitz model of risk return optimization

Capital Asset Pricing Model (CAPM)

Arbitrage Pricing Theory (APT)

Sharpe Index Model

Portfolio Management - Formulation, Monitoring and Evaluation

Equity Style Management

Principles and Management of Hedge Funds

International Portfolio Management.

8. Financial Services in India

Investment Banking

Retail Banking

On Line Share Trading

Depository Service.

9. (a) Mutual Funds: Regulatory framework, formulation, monitoring and evaluation of various schemes of Mutual funds, Money market mutual funds.

(b) Exchange Traded Funds.

10. Money Market operations

11. (a) Foreign Direct Investment, Foreign Institutional Investment.

(b) International Financial Management

Raising of capital abroad - American Depository Receipts, Global Depository Receipts, External Commercial Borrowings and Foreign Currency Convertible Bonds

International Capital Budgeting

International Working Capital Management.

12. Foreign Exchange Exposure and Risk Management

Exchange rate determination, Exchange rate forecasting

Foreign currency market

Foreign exchange derivatives – Forward, futures, options and swaps

Management of transaction, translation and economic exposures

Hedging currency risk.

13. Mergers, Acquisitions and Restructuring

Meaning of mergers and acquisition, categories, purposes

Process of mergers and acquisition – Identification and valuation of the target, acquisition through negotiation, due diligence, post – merger integration

Legal and regulatory requirements

Merger and Acquisition agreement

Reverse merger

Potential adverse competitive effects of mergers

Corporate Takeovers: Motivations, Co-insurance effect, Cross-border takeovers, Forms of takeovers, Takeover defenses

Going Private and Other Control Transactions: Leveraged Buyouts (LBOs), Management Buyouts (MBOs), Spin Offs and Asset Divestitures

Corporate Restructuring : Refinancing and rescue financing, reorganizations of debtors and creditors, Sale of assets, targeted stock offerings, downsizing and layoff programmes, negotiated wage give-backs, employee buyouts.

PAPER – 3 : ADVANCED AUDITING AND PROFESSIONAL ETHICS

(One Paper- Three hours - 100 marks)

Level of Knowledge: Advanced knowledge

Objectives:

- (a) To gain expert knowledge of current auditing practices and procedures and apply them in auditing engagements,
- (b) To develop ability to solve cases relating to audit engagements.

Contents:

1. Auditing Standards, Statements and Guidance Notes

Auditing and Assurance Standards (AASs); Statements and Guidance Notes on Auditing issued by the ICAI; Significant differences between Auditing and Assurance Standards and International Standards on Auditing.

2. Audit strategy, planning and programming

Planning the flow of audit work; audit strategy, planning programme and importance of supervision: review of audit notes and working papers; drafting of reports; principal's ultimate responsibility; extent of delegation; control over quality of audit work; reliance on the work of other auditor, internal auditor or an expert.

3. Risk Assessment and Internal Control

Evaluation of internal control procedures; techniques including questionnaire, flowchart; internal audit and external audit, coordination between the two.

4. Audit under computerized information system (CIS) environment

Special aspects of CIS Audit Environment, need for review of internal control especially procedure controls and facility controls. Approach to audit in CIS Environment, use of computers for internal

and management audit purposes: audit tools, test packs, computerized audit programmes; Special Aspects in Audit of E-Commerce Transaction.

5. Special audit techniques
 - (a) Selective verification; statistical sampling: Special audit procedures; physical verification of assets, direct confirmation of debtors and creditors
 - (b) Analytical review procedures
 - (c) Risk-based auditing.
6. Audit of limited companies

Statutory requirements under the Companies Act 1956; Audit of branches: joint audits; Dividends and divisible profits % financial, legal, and policy considerations.
7. Rights, duties, and liabilities of auditors; third party liability.
8. Audit reports; qualifications, notes on accounts, distinction between notes and qualifications, detailed observations by the statutory auditor to the management vis-a-vis obligations of reporting to the members.
9. Audit Committee and Corporate Governance
10. Audit of Consolidated Financial Statements, Audit Reports and Certificates for Special Purpose engagements; Certificates under the Payment of Bonus Act, import/export control authorities, etc.; Specific services to non-audit clients; Certificate on Corporate Governance.
11. Special features of audit of banks, insurance companies, co-operative societies and non-banking financial companies.
12. Audit under Fiscal Laws, viz, Direct and Indirect Tax Laws.
13. Cost audit
14. Special audit assignments like audit of bank borrowers, audit of stock and commodity exchange intermediaries and depositories; inspection of special entities like banks, financial institutions, mutual funds, stock brokers.
15. Special features in audit of public sector companies. Directions of Comptroller and Auditor General of India under Section 619; Concepts of propriety and efficiency audit.
16. Internal audit, management and operational audit Nature and purpose, organisation, audit programme, behavioural problems; Internal Audit Standards issued by the ICAI; Specific areas of management and operational audit involving review of internal control, purchasing operations, manufacturing operations, selling and distribution, personnel policies, systems and procedures. Aspects relating to concurrent audit.
17. Investigation and Due Diligence.
18. Concept of peer review
19. Salient features of Sarbanes – Oxley Act, 2002 with special reference to reporting on internal control.
20. Professional Ethics

Code of Ethics with special reference to the relevant provisions of The Chartered Accountants Act, 1949 and the Regulations thereunder.

PAPER – 4 : CORPORATE AND ALLIED LAWS

(One paper – Three hours – 100 marks)

Section A : Company Law (70 Marks)

Level of Knowledge: Advanced knowledge

Objective:

To be able to analyze and apply various provisions of the Companies Act in practical situations

Contents:

1. The Companies Act, 1956, Rules and Regulations thereunder in its entirety with specific reference to
 - (a) Accounts and audit
 - (b) Dividend
 - (c) Directors - powers, managerial remuneration
 - (d) Meetings, powers of the Board and related party transactions
 - (e) Inspection and Investigation
 - (f) Compromises, Arrangements and Reconstructions
 - (g) Prevention of Oppression and Mismanagement
 - (h) Revival and Rehabilitation of Sick Industrial Companies
 - (i) Corporate Winding up and Dissolution
 - (j) Producer Companies
 - (k) Companies incorporated outside India
 - (l) Offences and Penalties
 - (m) E-governance
2. Corporate Secretarial Practice – Drafting of Resolution, Minutes, Notices and Reports

Section B : Allied Laws (30 Marks)

Objective:

To develop ability to analyse the requirements of laws stated in the Section.

Contents:

3. An overview of the following laws –
 - (a) The Securities and Exchange Board of India Act, 1992, Rules, Regulations and Guidelines issued thereunder.
 - (b) The Securities Contracts (Regulation) Act, 1956
 - (c) The Foreign Exchange Management Act, 1999
 - (d) The Competition Act, 2002
 - (e) The Banking Regulation Act, 1949, The Insurance Act, 1938. The Insurance Regulatory and Development Authority Act, 1999. The Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002
 - (f) The Prevention of Money Laundering Act, 2002
4. Interpretation of Statutes, Deeds and Documents.

PAPER – 5 : ADVANCED MANAGEMENT ACCOUNTING

(One paper – Three hours – 100 marks)

Level of Knowledge: Advanced knowledge

Objective:

To apply various management accounting techniques to all types of organizations for planning, decision making and control purposes in practical situations.

To develop ability to apply quantitative techniques to business problems

1. Cost Management

- (a) Developments in the business environment; just in time; manufacturing resources planning; (MRP); automated manufacturing; synchronous manufacturing and back flush systems to reflect the importance of accurate bills of material and routings; world class manufacturing; total quality management.
- (b) Activity based approaches to management and cost analysis
- (c) Analysis of common costs in manufacturing and service industry
- (d) Techniques for profit improvement, cost reduction, and value analysis
- (e) Throughput accounting
- (f) Target costing; cost ascertainment and pricing of products and services
- (g) Life cycle costing
- (h) Shut down and divestment.

2. Cost Volume Profit Analysis

- (a) Relevant cost
- (b) Product sales pricing and mix
- (c) Limiting factors
- (d) Multiple scarce resource problems
- (e) Decisions about alternatives such as make or buy, selection of products, etc.

3. Pricing Decisions

- (a) Pricing of a finished product
- (b) Theory of price
- (c) Pricing policy
- (d) Principles of product pricing
- (e) New product pricing
- (f) Pricing strategies
- (g) Pricing of services
- (h) Pareto analysis

4. Budgets and Budgetary Control

The budget manual, Preparation and monitoring procedures, Budget variances, Flexible budgets, Preparation of functional budget for operating and non-operating functions, Cash budgets, Capital expenditure budget, Master budget, Principal budget factors.

5. Standard Costing and Variance Analysis

Types of standards and sources of standard cost information; evolution of standards, continuous - improvement; keeping standards meaningful and relevant; variance analysis; disposal of variances.

- (a) Investigation and interpretation of variances and their inter relationship
- (b) Behavioural considerations.
- 6. Transfer pricing
 - (a) Objectives of transfer pricing
 - (b) Methods of transfer pricing
 - (c) Conflict between a division and a company
 - (d) Multi-national transfer pricing.
- 7. Cost Management in Service Sector
- 8. Uniform Costing and Inter firm comparison
- 9. Profitability analysis - Product wise / segment wise / customer wise
- 10. Financial Decision Modeling
 - (a) Linear Programming
 - (b) Network analysis - PERT/CPM, resource allocation and resource leveling
 - (c) Transportation problems
 - (d) Assignment problems
 - (e) Simulation
 - (f) Learning Curve Theory
 - (g) Time series forecasting
 - (h) Sampling and test of hypothesis

PAPER – 6 : INFORMATION SYSTEMS CONTROL AND AUDIT

(One Paper – Three hours – 100 marks)

Level of knowledge: Advanced knowledge

Objective:

To gain application ability of necessary controls, laws and standards in computerized Information system.

Contents:

1. Information Systems Concepts
 - General Systems Concepts – Nature and types of systems, nature and types of information, attributes of information.
 - Management Information System – Role of information within business
 - Business information systems –various types of information systems – TPC, MIS, DSS, EIS, ES
2. Systems Development Life Cycle Methodology
 - Introduction to SDLC/Basics of SDLC
 - Requirements analysis and systems design techniques
 - Strategic considerations : Acquisition decisions and approaches
 - Software evaluation and selection/development
 - Alternate development methodologies- RAD, Prototype etc
 - Hardware evaluation and selection
 - Systems operations and organization of systems resources

Systems documentation and operation manuals
 User procedures, training and end user computing
 System testing, assessment, conversion and start-up
 Hardware contracts and software licenses
 System implementation
 Post-implementation review
 System maintenance
 System safeguards
 Brief note on IS Organisation Structure

3. Control objectives

(a) Information Systems Controls

Need for control
 Effect of computers on Internal Audit
 Responsibility for control – Management, IT, personnel, auditors
 Cost effectiveness of control procedure
 Control Objectives for Information and related Technology (COBIT)

(b) Information Systems Control Techniques

Control Design: Preventive and detective controls, Computer-dependent control, Audit trails, User Controls (Control balancing, Manual follow up)
 Non-computer-dependent (user) controls: Error identification controls, Error investigation controls, Error correction controls, Processing recovery controls

(c) Controls over system selection, acquisition/development

Standards and controls applicable to IS development projects
 Developed / acquired systems
 Vendor evaluation
 Structured analysis and design
 Role of IS Auditor in System acquisition/selection

(d) Controls over system implementation

Acceptance testing methodologies
 System conversion methodologies
 Post implement review
 Monitoring, use and measurement

(e) Control over System and program changes

Change management controls
 Authorization controls
 Documentation controls
 Testing and quality controls
 Custody, copyright and warranties
 Role of IS Auditor in Change Management

- (f) Control over Data integrity, privacy and security
 - Classification of information
 - Logical access controls
 - Physical access controls
 - Environmental controls
 - Security concepts and techniques – Cryptosystems, Data Encryption Standards (DES), Public Key Cryptography & Firewalls
 - Data security and public networks
 - Monitoring and surveillance techniques
 - Data Privacy
 - Unauthorised intrusion, hacking, virus control
 - Role of IS Auditor in Access Control
- 4. Audit Tests of General and Automated Controls
 - (a) Introduction to basics of testing (reasons for testing);
 - (b) Various levels/types of testing such as: (i) Performance testing, (ii) Parallel testing, (iii) Concurrent Audit modules/Embedded audit modules, etc.
- 5. Risk assessment methodologies and applications: (a) Meaning of Vulnerabilities, Threats, Risks, Controls, (b) Fraud, error, vandalism, excessive costs, competitive disadvantage, business, interruption, social costs, statutory sanctions, etc. (c) Risk Assessment and Risk Management, (d) Preventive/detective/corrective strategies
- 6. Business Continuity Planning and Disaster recovery planning: (a) Fundamentals of BCP/DRP, (b) Threat and risk management, (c) Software and data backup techniques, (d) Alternative processing facility arrangements, (e) Disaster recovery procedural plan, (f) Integration with departmental plans, testing and documentation, (g) Insurance
- 7. An over view of Enterprise Resource Planning (ERP)
- 8. Information Systems Auditing Standards, guidelines, best practices (BS7799, HIPPA, CMM etc.)
- 9. Drafting of IS Security Policy, Audit Policy, IS Audit Reporting - a practical perspective
- 10. Information Technology Act, 2000

PAPER – 7: DIRECT TAX LAWS

(One paper – Three hours – 100 marks)

Level of Knowledge: Advanced knowledge

Objectives:

- (a) To gain advanced knowledge of the provisions of direct tax laws,
- (b) To acquire the ability to apply the knowledge of the provisions of direct tax laws to various situations in actual practice.

Contents:

- I. The Income-tax Act, 1961 and Rules thereunder (90 marks)
- II. The Wealth-tax Act, 1957 and Rules thereunder (10 marks)

While covering the direct tax laws, students should familiarise themselves with considerations relevant to tax management. These may include tax considerations with regard to specific management decisions, foreign collaboration agreements, international taxation, amalgamations,

tax incentives, personnel compensation plans, inter-relationship of taxation and accounting, with special reference to relevant accounting standards and other precautions to be observed to maximise tax relief. Further, they should have a basic understanding about the ethical considerations in tax management and compliance with taxation laws.

Note – If new legislations are enacted in place of the existing legislations relating to income tax and wealth tax, the syllabus will accordingly include such new legislations in the place of the existing legislations with effect from the date to be notified by the Institute.

PAPER – 8 : INDIRECT TAX LAWS

(One paper – Three hours – 100 marks)

Level of Knowledge: Advanced knowledge

Objectives:

- (a) To gain expert knowledge of the principles of the laws relating to central excise customs and service tax,
- (b) To acquire the ability to apply the knowledge of the provisions of the above-mentioned laws to various situations in actual practice.

Contents:

Section A : Central Excise (40 marks)

Central Excise Act, 1944 and the related Rules, Circulars and Notifications; Central Excise Tariff Act, 1985 and the related Rules.

Section B : Service tax & VAT (40 marks)

Law relating to service tax as contained in the Finance Act, 1994 as amended from time to time and the related Rules, Circulars and Notifications.

Issues related to Value Added Tax:

1. Backdrop for State-Level VAT in India
2. Taxonomy of VAT
3. Input tax credit, tax invoices
4. Small dealers and composition scheme
5. VAT procedures
6. VAT in relation to incentive schemes, works contract, lease transactions and hire purchase transactions.
7. VAT and Central Sales Tax

Section C : Customs (20 marks)

Customs Act, 1962 and the related Rules, Circulars and Notifications; Customs Tariff Act, 1975 and the related Rules.

While covering the above laws, students should familiarize themselves with the inter-relationship of accounting with excise, customs and service tax and also the ethical considerations involved in the compliance of these laws.

Note – If new legislations are enacted in place of the existing legislations relating to central excise, customs and service tax, the syllabus will accordingly include such new legislations in place of the existing legislations with effect from the date to be notified by the Institute. Students shall not be examined with reference to any particular State VAT Law.

TRANSITION SCHEME FOR FINAL STUDENTS

The transition scheme for the Final Course students, who have passed Professional Education (Examination-II), and are under articleship training, is as under:

- ◆ On completion of 2 years of training, such students are eligible to appear in the Final Examination, so long as the same is held under the existing syllabus i.e., upto November, 2009.

In the event of a candidate not being eligible to appear till the last Final Examination to be held in November 2009 under the existing syllabus, will be required to appear in the Final Examination under the New syllabus, but only during the last six months of articleship training (articleship training period being 3 years only).

Introduction of Final Course under New Syllabus and other related Issues

- (i) Final Course under New syllabus is introduced. Admission to the Final (New) Course under the Regulation 29B of the Chartered Accountants (Amendment) Regulations, 2006 has commenced on and from February 1, 2007.
- (ii) Existing students of Final (old) course may switch over to Final (New) course and continue with the existing scheme of articleship, if any, which they are undergoing. They will be provided a new set of study materials at a cost of Rs.1100.
- (iii) Students, who have passed the Professional Education (Examination-II) / Intermediate Examination but not yet joined Final course and also have not completed the articleship training, may join the Final (New) Course.
 - ◆ Students who have undergone Professional Education (Course-II) with articleship but not yet completed the same, will continue the articleship under the same scheme which they are undergoing presently. They will be allowed to appear in the Final Examination under the new syllabus pending last six months of articleship training on or before the last day of the month preceding the month in which the examination is held.
 - ◆ Students who have undergone Professional Education (Course-II), without articleship, will undergo three years of articleship training and they will be allowed to appear in the Final Examination under the new syllabus pending last six months of articleship training on or before the last day of the month preceding the month in which the examination is held.

They will be required to pay fees as given below:

Final Course – Without articleship Rs.8500

With articleship Rs.9000 (including articulated registration fee of Rs.500)

In addition, students have to pay Rs.500 on account of registration fee with Board of Studies and Rs.500 on account of Students' Association fee if these fees are not paid earlier.

- (iv) Students who have passed Professional Education (Examination-II) / Intermediate Examination and who have completed articleship training may join Final (New) course under Regulation 29B of the Chartered Accountants (Amendment) Regulations, 2006 and appear in the first Final (New) Course Examination to be held in November, 2008. They will be required to pay a fee of Rs.8500.
- (v) Admission to Final (old) course under Regulation 29A of the Chartered Accountants Regulations, 1988 will continue till October 31, 2007. Students who will join the same are required to pay the following fees:

Final Course	– Without articleship	Rs.4000
	– With articleship	Rs.4600
- (vi) First Final Examination (New) Course will be held in November, 2008 and Last Final Examination (Old) Course will be held in November, 2009.
- (vii) Students shall complete 100 Hours Information Technology Training or should have already completed 250 Hours Compulsory Computer Training before taking admission to Final (Old) or Final (New) Course.

APPLICABILITY OF VARIOUS PUBLICATIONS FOR FINAL EXAMINATION TO BE HELD IN NOVEMBER 2007

Paper 1 : Advanced Accounting

- I. Statements and Standards
 1. Framework for the Preparation and Presentation of Financial Statements
 2. Accounting Standards – AS 1 to AS 29 [including revised AS 15 (2005)].
- II. Guidance Notes on Accounting Aspects
 1. Guidance Note on Treatment of Reserve Created on Revaluation of Fixed Assets.
 2. Guarantees and Counter-Guarantees Given by Companies.
 3. Guidance Note on Treatment of Expenditure during Construction Period.
 4. Guidance Note on Accrual Basis of Accounting.
 5. Guidance Note on Accounting Treatment for Excise Duty.
 6. Guidance Note on Accounting for Depreciation in Companies.
 7. Guidance Note on Availability of Revaluation Reserve for Issue of Bonus shares.
 8. Guidance Note on Accounting Treatment for MODVAT/CENVAT.
 9. Guidance Note on Accounting for Securitisation.
 10. Guidance Note on Accounting for Equity Index and Equity Stock Futures and Options (2003).
 11. Guidance Note on Accounting for Corporate Dividend Tax.
 12. Guidance Note on Accounting for Investments in the Financial Statements of Mutual Funds.
 13. Guidance Note on Accounting for Employee Share-based Payments.
 14. Guidance Note on Accounting for Fringe Benefits Tax.
 15. Guidance Note on Accounting for Credit Available in respect of Minimum Alternate Tax under the Income Tax Act, 1961.

Paper 3 : Advanced Auditing

- I. Professional Topics/Subjects
 1. Code of Ethics

The Chartered Accountants (Amendment) Act, 2006 is applicable for November, 2007 Final Examination. Questions on Professional Ethics may be asked in accordance with the Chartered Accountants (Amendment) Act, 2006. Chapter 17 of Advanced Auditing of Final (Old) Course study material should be accordingly read with appropriate amendments.

A supplementary study material is released covering Chapter 17 of Advanced Auditing study material. The supplementary study material can also be downloaded from the website www.icaai.org > Students > Courses (Course Curriculum) > Final > Supplementary Study Materials > Advanced Auditing.
- II. Statements and Standards
 1. Framework of Statements on Standard Auditing Practices and Guidance Notes on Related Services.
 2. Auditing and Assurance Standards AAS 1 to AAS 34
 3. Statement on Qualifications in Auditor's Report
 4. Statement on the Companies (Auditor's Report) Order, 2003 [2005 Edition].

III. Guidance Notes/Study Guide/Monograph

Guidance Notes on Auditing Aspects:

1. Guidance Note on Independence of Auditors
2. Internal Control Questionnaire.
3. Guidance Note on Accountant's Report on Profit Forecasts and / or Financial Forecasts.
4. Guidance Note on Audit Reports and Certificates for Special Purposes
5. Guidance Note on Audit of Fixed Assets.
6. Guidance Note on Audit under Section 44AB of the Income Tax Act [2005 Edition].
7. Guidance Note on Audit of Abridged Financial Statements.
8. Guidance Note on Audit of Inventories.
9. Guidance Note on Audit of Debtors, Loans and Advances.
10. Guidance Note on Audit of Investments.
11. Guidance Note on Audit of Miscellaneous Expenditure.
12. Guidance Note on Audit of Cash and Bank Balances.
13. Guidance Note on Audit of Liabilities.
14. Guidance Note on Audit of Revenue.
15. Guidance Note on Audit of Expenses.
16. Guidance Note on Section 227 (3) (e) and (f) of the Companies Act, 1956.
17. Guidance Note on Certificate of Corporate Governance [2006 Edition].
18. Guidance Note on Revision of Audit Report.
19. Guidance Note on Computer Assisted Audit Techniques (CAATs).
20. Guidance Note on Audit of Payment of Dividend.
21. Guidance Note on Audit of Capital and Reserves.

Paper 4 : Corporate Laws and Secretarial Practice

May, 2007 edition is relevant for November, 2007 Examination. Amendments in the SEBI (DIP) Guidelines 2000 as amended up to 30th April, 2007 may be made applicable.

Paper 7 : Direct Taxes

1. Study Material for Direct Taxes (as amended by Finance Act, 2006) – June 2006 edition. The relevant assessment year is A.Y.2007-08.
2. Select cases in Direct and Indirect Taxes (2006) – An Essential reading for the Final Course.[Portions relating to Direct Taxes]
3. Final Course – Supplementary Study Paper – 2006 Direct Taxes and Indirect Taxes – Amendments made by the Finance Act, 2006. [Portions relating to Direct Taxes]. This publication is relevant for those who have any earlier edition (prior to June 2006 edition) of the Direct Taxes study material.

Note – For the purposes of setting the questions in direct taxes, study material for A.Y.2007-08 containing the law as amended by the Finance Act, 2006 should be taken into account. This study material contains amendments made by notifications/circulars/other legislations up to 30.04.2006. The amendments made between 1.05.2006 and 30.4.2007 would be published in the Revision Test Papers

for November, 2007 examination. All these amendments are relevant for November, 2007 examination and hence should be taken into account for the purpose of setting questions for this exam.

Paper 8 : Indirect Taxes

1. Study Material for Indirect Taxes (as amended by Finance Act, 2006).
2. Select cases in Direct and Indirect Taxes (2006) – An Essential reading for the Final Course [Portions relating to Indirect Taxes]
3. Final Course – Supplementary Study Paper – 2006 Direct Taxes and Indirect Taxes – Amendments made by the Finance Act, 2006 [Portions relating to Indirect Taxes]. This publication is relevant for those who have any earlier Indirect Taxes Study Material (prior to the one as amended by Finance Act, 2006).

Note – For the purposes of setting the questions in indirect taxes, study material containing the law as amended by the Finance Act, 2006 should be taken into account. This study material contains amendments made by notifications/circulars/other legislations up to 30.04.2006. The amendments made between 1.05.2006 and 30.4.2007 would be published in the Revision Test Papers for November 2007 examination. All these amendments are relevant for November 2007 examination and hence should be taken into account for the purpose of setting questions for this exam.

RECENT PUBLICATIONS OF THE BOARD OF STUDIES

	English Rs.	Hindi Rs.	Postal Charges By Registered Parcel	
			English Rs.	Hindi Rs.
I. STUDY MATERIALS				
COMMON PROFICIENCY TEST (CPT)				
Fundamentals of Accounting	200	140		
Mercantile Laws	50	40		
General Economics	100	70		
Quantitative Aptitude	250	150		
Self Assessment CD	<u>40</u>	<u>40</u>		
	<u>640</u>	<u>440</u>	145	145
PROFESSIONAL COMPETENCE COURSE (PCC)				
Group I				
Advanced Accounting Vol. I & Vol. II	500	500		
Auditing and Assurance Vol. I	175	175		
Auditing & Assurance Standards & Guidance Note (English) Vol. II	100			
Law, Ethics and Communication	<u>275</u>	<u>275</u>		
	<u>1050</u>	<u>950</u>	215	215
Group II				
Cost Accounting & Financial Management	300	300		
Taxation	200	200		
Information Technology	150	150		
Strategic Management	<u>100</u>	<u>100</u>		
	<u>750</u>	<u>750</u>	180	180
Both Groups	<u>1800</u>	<u>1700</u>	395	395
FINAL (NEW COURSE)				
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Financial Reporting	600			
Strategic Financial Management	260			
Advanced Auditing and Professional Ethics	520			
Corporate and Allied Laws	<u>200</u>			
	<u>1580</u>		320	
Group II				
Advanced Management Accounting	240			
Information Systems Control and Audit	150			
Direct Tax Laws	340			
Indirect Tax laws	<u>290</u>			
	<u>1020</u>		225	
Both Groups	2600		540	
Information Technology Training Course Material				
Information Technology Training Programme - Modules I & II	500		90	
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Paper 4 A: Cost Accounting (May, 1981 – November, 2006)	60	40
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Final		
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– With Form Nos. 102 and 103	100	40
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2. Model Test Paper Vol. I for PCC	50	36
3. Students Guide to Accounting Standard 28: Impairment of Assets	25	36
4. Supplementary Study Paper-2006 Income tax & Central Sales Tax for PE(Course-II)	30	40
5. Supplementary Study Paper -2006 Direct tax and Indirect tax for Final Course	60	40
6. Select cases Direct and Indirect Taxes – 2006 For Final Course	40	40
7. Supplementary Study paper – 2007 Advanced Auditing for Final Course	60	40
8. Training Guide	80	40
9. Information Brochure about Common Proficiency Test – A Simplified Entry to the Chartered Accountancy Course Both in English and Hindi		
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