

PAPER – 4 : COST ACCOUNTING AND FINANCIAL MANAGEMENT

Question No. 1 and 6 are compulsory.

Answer any three questions from the rest.

Working notes should form part of the answer.

Question 1

- (a) Following details are related to the work done in Process 'A' of XYZ Company during the month of March, 2007:

Opening work-in-progress (2,000 units)	Rs.
Materials	80,000
Labour	15,000
Overheads	45,000
Materials introduced in Process 'A' (38,000 units)	14,80,000
Direct labour	3,59,000
Overheads	10,77,000
Units scrapped: 3,000 units	
Degree of completion:	
Materials	100%
Labour and overheads	80%
Closing work-in-progress : 2,000 units	
Degree of Completion:	
Materials	100%
Labour and overheads	80%

Units finished and transferred to Process 'B' : 35,000

Normal Loss:

5% of total input including opening work-in-progress

Scrapped units fetch Rs. 20 per piece.

You are required to prepare:

- (i) Statement of equivalent production;
- (ii) Statement of cost;
- (iii) Statement of distribution cost; and
- (iv) Process 'A' Account, Normal and Abnormal Loss Accounts.

(b) Explain briefly each of the following categories in Activity based Costing by giving at least two examples:

- (i) Unit level activities
- (ii) Batch level activities
- (iii) Product level activities
- (iv) Facility level activities.

(10 + 8 = 18 Marks)

Answer

(a)

Statement of Equivalent Production

Input	Units	Output	Units	Equivalent production			
				Material		Labour & Overheads	
				%	Units	%	Units
Opening WIP	2,000	Completed and transfer to Process 'B'	35,000	100	35,000	100	35,000
Units introduced	38,000	Normal loss (5% of 40,000)	2,000		—		—
		Abnormal loss	1,000	100	1,000	80	800
		Closing WIP	<u>2,000</u>	100	<u>2,000</u>	80	<u>1,600</u>
	<u>40,000</u>		<u>40,000</u>		<u>38,000</u>		<u>37,400</u>

(ii)

Statement of Cost

Details	Cost at the beginning of process	Cost added	Total cost	Equivalent Units	Cost per unit
	Rs.	Rs.	Rs.	Rs.	Rs.
Material	80,000	14,80,000	15,60,000		
Less: Value of normal loss			<u>(20 × 2,000 = 40,000)</u>	38,000	40
			15,20,000		
Labour	15,000	3,59,000	3,74,000	37,400	10
Overheads	45,000	10,77,000	11,22,000	37,400	<u>30</u>
					<u>80</u>

(iii) Statement of distribution of cost:

- (a) Completed and transferred to process 'B' = 35,000 units @Rs. 80 = Rs. 28,00,000.
- (b) Abnormal loss : 1,000 units:

Materials 1,000 units @ 40 = Rs. 40,000

Labour and Overheads 800 units @ 40 = Rs. 32,000

Rs. 72,000

(c) Closing WIP : 2,000 units

Materials 2,000 units @ 40 = Rs. 80,000

Labour and Overheads 1,600 units @ 40 = Rs. 64,000

Rs. 1,44,000

(iv) Process 'A' Account

Dr.				Cr.			
Particulars	Units	Amount	Particulars	Units	Amount		
To Opening WIP	2,000	1,40,000*	By Normal Loss	2,000	40,000		
Material introduced	38,000	14,80,000	By Abnormal loss	1,000	72,000		
Direct labour		3,59,000	By Process 'B' A/c transfer to next process	35,000	28,00,000		
Overheads		10,77,000					
			By Closing WIP				
				2,000	1,44,000		
				<u>40,000</u>	<u>30,56,000</u>		
				<u>40,000</u>	<u>30,56,000</u>		

*Materials + Labour + Overheads = Rs. (80,000 + 15,000 + 45,000) = Rs.1,40,000.

Normal Loss Account

Dr.				Cr.			
To Process 'A' A/c	<u>2,000</u>	<u>40,000</u>	By By Cost Ledger Control A/c	<u>2,000</u>	<u>40,000</u>		
	<u>2,000</u>	<u>40,000</u>		<u>2,000</u>	<u>40,000</u>		

Abnormal Loss Account

Dr.				Cr.			
To Process 'A' A/c	1,000	72,000	By By Cost Ledger Control A/c	1,000	20,000		
			By Costing Profit and Loss A/c		<u>52,000</u>		
	<u>1,000</u>	<u>72,000</u>		<u>1,000</u>	<u>72,000</u>		

(b) (i) Unit level activities – The cost of some activities (mainly primary activities) are strongly co-related to the number of units produced. These activities are known as unit level activities. Examples are:

(a) The use of indirect materials.

(b) Inspection or testing of every item produced or say every 100th item produced.

(c) Indirect consumables.

- (ii) Batch level activities – The cost of some activities (mainly manufacturing support activities) are driven by the number of batches of units produced. These activities are known as Batch level activities. Examples are:
- (a) Material ordering.
 - (b) Machine set up cost.
 - (c) Inspection of products - like first item of every batch.
- (iii) Product level activities – The cost of some activities are driven by the creation of a new product line and its maintenance. These activities are known as Product level activities. Examples are:
- (a) Designing the product.
 - (b) Producing parts to a certain specified limit.
 - (c) Advertising cost, if advertisement is for individual products.
- (iv) Facility level activities – The cost of some activities cannot be related to a particular product line, instead they are related to maintaining the building and facilities. These activities are known as Facility level activities. Examples are:
- (a) Maintenance of buildings.
 - (b) Plant security.
 - (c) Production manager's salary.
 - (d) Advertising campaigns promoting the company.

Question 2

- (a) What is 'Integrated Accounting System'? State its advantages.
- (b) A Club runs a library for its members. As part of club policy, an annual subsidy of upto Rs. 5 per member including cost of books may be given from the general funds of the club. The management of the club has provided the following figures for its library department.

Number of Club members	5,000
Number of Library members	1,000
Library fee per member per month	Rs. 100
Fine for late return of books	Re. 1 per book per day
Average No. of books returned late per month	500
Average No. of days each book is returned late	5 days
Number of available old books	50,000 books
Cost of new books	Rs. 300 per book
Number of books purchased per year	1,200 books
Cost of maintenance per old book per year	Rs. 10

Staff details	No.	Per Employee Salary per month (Rs.)
Librarian	01	10,000
Assistant Librarian	03	7,000
Clerk	01	4,000

You are required to calculate:

- the cost of maintaining the library per year excluding the cost of new books;
- the cost incurred per member per month on the library excluding cost of new books; and
- the net income from the library per year.

If the club follows a policy that all new books must be purchased out of library revenue (a) What is the maximum number of books that can be purchased per year and (b) How many excess books are being purchased by the library per year?

Also, comment on the subsidy policy of the club. (4 + 10 = 14 Marks)

Answer

(a) Integrated Accounting System:

It is such a system of accounting whereby cost and financial accounts are kept in the same set of books. Obviously, then there will be no separate set of books for costing and financial records. Integrated accounts provide or meets out fully the information requirements for costing as well as financial accounts.

Advantages of Integrated Accounting System:

- The question of reconciling of costing and financial profits does not arise, as there is one figure of profit only.
- Due to use of one set of books, there is significant extent of saving in efforts made.
- No delay is caused in obtaining information as it is provided from books of original entry.
- It is economical as it is based on the concept of centralisation of Accounting function.

(b) Computation of total revenue

No. of library members	No	<u>1,000</u>
Library fees per month	Rs.	1,00,000
Late fees per month (500 × 5 × 1)	Rs.	<u>2,500</u>
Total Revenue per month	Rs.	<u>1,02,500</u>
Total Revenue per annum (1,02,500 × 12)	Rs.	<u>12,30,000</u>

Computation of total cost

Staff details	No.	Salary per month	Total cost
		Rs.	Rs.
Librarian	1	10,000	10,000
Assistant Librarian	3	7,000	21,000
Clerk	1	4,000	<u>4,000</u>
Total Staff cost per month			<u>35,000</u>
Total Staff cost per year (35,000 × 12)			<u>4,20,000</u>
	No.	Cost per book	
Books maintenance cost	50,000	Rs. 10	<u>5,00,000</u>
Total maintenance cost per annum excluding cost of new books (4,20,000 + 5,00,000)			<u>9,20,000</u>

Cost incurred per library member per annum

(Rs. 9,20,000/1,000)	Rs.	920
Cost incurred per member per month on the library excluding cost of new books (920/12)	Rs.	76.67
Cost incurred per club member per annum (9,20,000/5,000)	Rs.	184
Cost incurred per club member per month (184/12)	Rs.	15.33
Net income from the library per annum (12,30,000 – 9,20,000)	Rs.	<u>3,10,000</u>
Cost per new book	Rs.	300
Maximum number of new books per annum (3,10,000/300)	No.	1033.333
Present number of books purchased	No.	1200
Excess books purchased (1200 – 1033.333)	No.	166.6667
Subsidy being given per annum	Rs.	50,000
Subsidy per library member per annum (50,000/1,000)	Rs.	50
Subsidy per club member per annum (50,000/5,000)	Rs.	10

Comment:

The club is exceeding its subsidy target to members by Rs. 45 (Rs. 50 – 5) per library member and Rs. 5 (Rs. 10 – 5) per club member.

Question 3

- (a) Raw materials 'AXE' costing Rs. 150 per kg. and 'BXE' costing Rs. 90 per kg. are mixed in equal proportions for making product 'A'. The loss of material in processing works out to 25% of the product. The production expenses are allocated at 40% of direct material cost. The end product is priced with a margin of 20% over the total cost.

Material 'BXE' is not easily available and substitute raw material 'CXE' has been found for 'BXE' costing Rs. 75 per kg. It is required to keep the proportion of this substitute material in the mixture as low as possible and at the same time maintain the selling price of the end product at existing level and ensure the same quantum of profit as at present.

You are required to compute the ratio of the mix of the raw materials 'AXE' and 'CXE'.

- (b) Answer any three of the following:

- (i) Explicit and Implicit Costs
- (ii) Period Costs and Discretionary Costs
- (iii) Efficiency Audit and Proprietary Audit
- (iv) Bin Cards and Stock Control Cards.

(8 + 6 = 14 Marks)

Answer

- (a) Working Notes:

- (i) Computation of material mix ratio:

Let 1 kg. of product A requires 1.25 kg. of input of materials A X E and B X E

Raw materials are mixed in equal proportions.

$$\text{Then raw material A X E} = \frac{1.25}{2} = .625 \text{ kg.}$$

$$\text{Then raw material B X E} = \frac{1.25}{2} = .625 \text{ kg.}$$

- (ii) Computation of selling price / kg. of product A

	Rs.
Raw material A X E .625 kg. × 150 = Rs. 93.75	
Raw material B X E .625 kg. × 90 = <u>Rs. 56.25</u>	150.00
Production expenses (40% of material cost)	<u>60.00</u>
Total cost	210.00

Add: profit 20% of total cost	<u>42.00</u>
Selling price	<u>252.00</u>

Computation of proportions of materials A X E and C X E in 'A'

Let material C X E required in product A be m kg.

Then for producing 1 kg of product 'A', material A X E requirement = (1.25 – m) kg.

To maintain same level of profit and selling price as per Working note (ii), it is required that the total cost of material in 1 kg. of product A should not exceed Rs. 150,

$$\text{i.e., } m \text{ kg.} \times \text{Rs. } 75 + (1.25 - m) \text{ kg.} \times 150 = \text{Rs. } 150$$

$$\text{or } 75m + 187.5 - 150m = 150$$

$$\text{or } 75m = 37.5$$

$$\text{or } m = 0.5 \text{ kg.}$$

Raw material A X E requirement in product A = 1.25 – .5 = .75 kg.

So, proportion of material A X E and C X E

$$= .75 : .50$$

$$\text{i.e. } 3 : 2.$$

(b) (i) Explicit and Implicit cost:

Explicit costs, which are also known as out of pocket costs, refer to costs involving immediate payment of cash. Salaries, wages, interest on loan etc. are examples of explicit costs. They can be easily measured.

The main points of difference between explicit and implicit costs are:

- Implicit costs do not involve immediate cash payment.
- They are not recorded in the books of account.
- They are also known as economic costs.

(ii) Period and Discretionary costs

There are the costs, which are not assigned to the products but are charged as expenses against the revenue of the period in which they are incurred. All non-manufacturing costs such as general and administrative expenses, selling and distribution expenses are period costs.

Such costs are not tied to a clear cause and effect relationship between inputs and outputs. They arise from periodic decisions regarding the maximum outlay to be incurred. Examples are – advertising, public relations, training etc.

(iii) Efficiency audit and Propriety audit:

Efficiency audit is directed towards the measurement of whether corporate plans have been effectively executed. It is concerned with the utilisation of resources in economic and most remunerative manner to achieve the objectives of the concern e.g. the effective utilisation of capital in an organisation can be gauged by determining return on capital employed.

Propriety audit is concerned with executive actions and plans bearing on the finances and expenditure of the company. The auditor has to judge whether the planned expenditure is designed to give optimum results.

(iv) Bin Cards and Stores control cards:

Bin Cards are quantitative records of the stores receipt, issue and balance. It is kept for each and every item of stores by the store keeper. Here, the balance is taken out after each receipt or issue transaction

Stock control cards are also similar to Bin Cards. Stock control cards contain further informations as regards stock on order. These cards are kept in cabinets or trays or loose binders.

Question 4

- (a) A company runs a holiday home. For this purpose, it has hired a building at a rent of Rs. 10,000 per month alongwith 5% of total taking. It has three types of suites for its customers, viz., single room, double rooms and triple rooms.

Following information is given:

Type of suite	Number	Occupancy percentage
Single room	100	100%
Double rooms	50	80%
Triple rooms	30	60%

The rent of double rooms suite is to be fixed at 2.5 times of the single room suite and that of triple rooms suite as twice of the double rooms suite.

The other expenses for the year 2006 are as follows:

	Rs.
Staff salaries	14,25,000
Room attendants' wages	4,50,000
Lighting, heating and power	2,15,000
Repairs and renovation	1,23,500
Laundry charges	80,500
Interior decoration	74,000
Sundries	1,53,000

Provide profit @ 20% on total taking and assume 360 days in a year.

You are required to calculate the rent to be charged for each type of suite.

- (b) 'Under the Rowan Premium Bonus system, a less efficient worker can obtain same bonus as a highly efficient worker.' Discuss with suitable examples. (10 + 4 = 14 Marks)

Answer

(a) (i) Total equivalent single room suites		
Nature of suite	Occupancy	Equivalent single room suites
Single room suites	$100 \times 360 \times 100\% = 36,000$	$36,000 \times 1 = 36,000$
Double rooms suites	$50 \times 360 \times 80\% = 14,400$	$14,400 \times 2.5 = 36,000$
Triple rooms suites	$30 \times 360 \times 60\% = 6,480$	$6,480 \times 5 = \underline{32,400}$
	Total	<u>1,04,400</u>

- (ii) Statement of total cost:

	Rs.
Staff salaries	14,25,000
Room attendant's wages	4,50,000
Lighting, heating and power	2,15,000
Repairs and renovation	1,23,500
Laundry charges	80,500
Interior decoration	74,000
Sundries	<u>1,53,000</u>
	25,21,000
Building rent $10,000 \times 12 + 5\%$ on total taking	1,20,000
	<u>+ 5% on takings</u>
Total cost	26,41,000 + 5% on total takings

Profit is 20% of total takings

$\therefore$ Total takings = Rs. 26,41,000 + 25% of total takings

Let x be rent for single room suite

Then $1,04,400 x = 26,41,000 + 25\%$ of $(1,04,400 x)$

or $1,04,400 x = 26,41,000 + 26,100 x$

or $78,300 x = 26,41,000$

or $x = 33.73$

(ii) Rent to be charged for single room suite = Rs. 33.73

Rent for double rooms suites Rs. $33.73 \times 2.5 = \text{Rs. } 84.325$

Rent for triple rooms suites Rs. $33.73 \times 5 = \text{Rs. } 168.65$

(b) Bonus under Rowan system = $\frac{\text{Time taken}}{\text{Time allowed}} \times \text{time saved} \times \text{rate per hour}$

For example let time allowed for a job = 4 hours and Labour rate = Rs. 5 per hour.

Case I : Less efficient worker

If time taken = 3 hours

Then time saved = $4 - 3 = 1$ hour

Bonus = $\frac{3 \text{ hours}}{4 \text{ hours}} \times 1 \text{ hour} \times \text{Rs. } 5 = \text{Rs. } 3.75$

Case II : Highly efficient worker

If time taken = 1 hour

Then time saved = $4 - 1 = 3$ hours

Bonus = $\frac{1 \text{ hour}}{4 \text{ hours}} \times 3 \text{ hours} \times \text{Rs. } 5 = \text{Rs. } 3.75$

So, it can be concluded that under Rowan System, the less efficient worker and highly efficient worker can get the same bonus.

Question 5

(a) ABC Ltd. has furnished the following information from the financial books for the year ended 31st March, 2007:

Profit & Loss Account

	Rs.		Rs.
To Opening stock		By Sales (10,250 units)	28,70,000
(500 units at Rs. 140 each)	70,000	By Closing stock	
Material consumed	10,40,000	(250 units at Rs. 200 each)	50,000
Wages	6,00,000		
Gross profit c/d	<u>12,10,000</u>		
	<u>29,20,000</u>		<u>29,20,000</u>

To	Factory overheads	3,79,000	By	Gross profit b/d	12,10,000
	Administration overheads	4,24,000		Interest	1,000
	Selling expenses	2,20,000		Rent received	40,000
	Bad debts	16,000			
	Preliminary expenses	20,000			
	Net profit	<u>1,92,000</u>			
		<u>12,51,000</u>			<u>12,51,000</u>

The cost sheet shows the cost of materials at Rs. 104 per unit and the labour cost at Rs. 60 per unit. The factory overheads are absorbed at 60% of labour cost and administration overheads at 20% of factory cost. Selling expenses are charged at Rs. 24 per unit. The opening stock of finished goods is valued at Rs. 180 per unit.

You are required to prepare:

- (i) A statement showing profit as per Cost accounts for the year ended 31st March, 2007; and
 - (ii) A statement showing the reconciliation of profit as disclosed in Cost accounts with the profit shown in Financial accounts.
- (b) Explain any two of the following:
- (i) Notional profit in Contract costing
 - (ii) Retention money in Contract costing
 - (iii) Economic Batch Quantity in Batch Costing. (10 + 4 = 14 Marks)

Answer

- (a) (i) Statement of profit as per cost accounts

	Units	Rs.
Opening stock @ Rs. 180 per unit	500	90,000
Cost of production @ Rs. 240 per unit (Refer Working Note 1)	<u>10,000</u>	<u>24,00,000</u>
Total	10,500	24,90,000
Less: Closing stock @ Rs. 240 per unit	<u>-250</u>	<u>-60,000</u>
	10,250	24,30,000
Selling expenses @ Rs. 24 per unit		<u>2,46,000</u>
Cost of sales		26,76,000
Profit		<u>1,94,000</u>
Sales	<u>10,250</u>	<u>28,70,000</u>

Working Notes:

(i) Statement of Cost (10,000 units)

	Total cost	Cost per unit
	Rs.	Rs.
Materials	10,40,000	104.00
Wages	6,00,000	60.00
Factory Overhead 60% of wages	<u>3,60,000</u>	<u>36.00</u>
Factory cost	20,00,000	200.00
Administrative overhead 20% of factory cost	<u>4,00,000</u>	<u>40.00</u>
Total cost	<u>24,00,000</u>	<u>240.00</u>

(ii) Statement of differences between the two set of accounts:

	Financial A/c	Cost A/c	Difference	Remarks
	Rs.	Rs.	Rs.	
Factory overhead	3,79,000	3,60,000	19,000	Under recovery
Administrative overhead	4,24,000	4,00,000	24,000	Under recovery
Selling expenses	2,20,000	2,46,000	26,000	Over recovery
Opening stock	70,000	90,000	20,000	Over recovery
Closing stock	50,000	60,000	10,000	Over recovery

(ii) Reconciliation Statement

	Rs.
Profit as per cost accounts	1,94,000
Less: Under recovery of Overhead in Cost A/c	
Factory Overhead	19,000
Administrative Overhead	<u>24,000</u>
	-43,000
Add: Over-recovery of selling overhead in Cost A/c	+26,000
Add: Over-valuation of opening stock in Cost A/c	+20,000
Less: Over-valuation of closing stock in Cost A/c	-10,000
Add: Income excluded from Cost A/c	
Interest	1,000
Rent	<u>40,000</u>
	+41,000

Less: Expenses excluded from Cost A/c

Bad debts	16,000	
Preliminary expenses	<u>20,000</u>	<u>-36,000</u>
Profit as per financial account		<u>1,92,000</u>

(b) (i) Notional profit in Contract costing:

It represents the difference between the value of work certified and cost of work certified.

Notional Profit = Value of work certified – (Cost of works to date – Cost of work not yet certified)

(ii) Retention Money in Contract Costing:

A contractor does not receive the full payment of the work certified by the surveyor. Contractee retains some amount to be paid after some time, when it is ensured that there is no default in the work done by the contractor. If any deficiency or defect is noticed, it is to be rectified by the contractor before the release of the retention money. Thus, the retention money provides a safeguard against the default risk in the contracts.

(iii) Economic Batch Quantity in Batch Costing

There are two types of costs involved in Batch Costing (i) set up costs (ii) carrying costs.

If the batch size is increased, set up cost per unit will come down and the carrying cost will increase. If the batch size is reduced, set up cost per unit will increase and the carrying cost will come down.

Economic Batch quantity will balance both these opponent costs. It is calculated as follows:

$$EBQ = \sqrt{\frac{2DS}{c}}$$

Where,

D = Annual Demand in units

S = Set up cost per batch

C = Carrying cost per unit per annum.

Question 6

- (a) The following accounting information and financial ratios of PQR Ltd. relate to the year ended 31st December, 2006:

	2006
I Accounting Information:	
Gross Profit	15% of Sales
Net profit	8% of sales
Raw materials consumed	20% of works cost
Direct wages	10% of works cost
Stock of raw materials	3 months' usage
Stock of finished goods	6% of works cost
Debt collection period	60 days
All sales are on credit	
II Financial Ratios:	
Fixed assets to sales	1 : 3
Fixed assets to Current assets	13 : 11
Current ratio	2 : 1
Long-term loans to Current liabilities	2 : 1
Capital to Reserves and Surplus	1 : 4

If value of fixed assets as on 31st December, 2005 amounted to Rs. 26 lakhs, prepare a summarised Profit and Loss Account of the company for the year ended 31st December, 2006 and also the Balance Sheet as on 31st December, 2006.

- (b) What is Debt securitisation? State the basic debt securitisation process.

(12 + 4 = 16 Marks)

Answer

- (a) Working Notes:

- (i) Calculation of Sales

$$\frac{\text{Fixed Assets}}{\text{Sales}} = \frac{1}{3}$$

$$\therefore \frac{26,00,000}{\text{Sales}} = \frac{1}{3} \Rightarrow \text{Sales} = \text{Rs.} 78,00,000$$

- (ii) Calculation of Current Assets

$$\frac{\text{Fixed Assets}}{\text{Current Assets}} = \frac{13}{11}$$

$$\therefore \frac{26,00,000}{\text{Current Assets}} = \frac{13}{11} \Rightarrow \text{Current Assets} = \text{Rs. } 22,00,000$$

(iii) Calculation of Raw Material Consumption and Direct Wages

	Rs.
Sales	78,00,000
Less: Gross Profit	<u>11,70,000</u>
Works Cost	<u>66,30,000</u>

Raw Material Consumption (20% of Works Cost) Rs. 13,26,000

Direct Wages (10% of Works Cost) Rs. 6,63,000

(iv) Calculation of Stock of Raw Materials (= 3 months usage)

$$= 13,26,000 \times \frac{3}{12} = \text{Rs. } 3,31,500$$

(v) Calculation of Stock of Finished Goods (= 6% of Works Cost)

$$= 66,30,000 \times \frac{6}{100} = \text{Rs. } 3,97,800$$

(vi) Calculation of Current Liabilities

$$\frac{\text{Current Assets}}{\text{Current Liabilities}} = 2$$

$$\frac{22,00,000}{\text{Current Liabilities}} = 2 \Rightarrow \text{Current Liabilities} = \text{Rs. } 11,00,000$$

(vii) Calculation of Debtors

$$\text{Average collection period} = \frac{\text{Debtors}}{\text{Credit Sales}} \times 365$$

$$\frac{\text{Debtors}}{78,00,000} \times 365 = 60 \Rightarrow \text{Debtors} = \text{Rs. } 12,82,191.78 \text{ or Rs. } 12,82,192$$

(viii) Calculation of Long term Loan

$$\frac{\text{Long term Loan}}{\text{Current Liabilities}} = \frac{2}{1}$$

$$\frac{\text{Long term loan}}{11,00,000} = \frac{2}{1} \Rightarrow \text{Long term loan} = \text{Rs. } 22,00,000.$$

(ix) Calculation of Cash Balance

		Rs.
Current assets		22,00,000
Less: Debtors	12,82,192	
Raw materials stock	3,31,500	
Finished goods stock	<u>3,97,800</u>	<u>20,11,492</u>
Cash balance		<u>1,88,508</u>

(x) Calculation of Net worth

Fixed Assets		26,00,000
Current Assets		<u>22,00,000</u>
Total Assets		48,00,000
Less: Long term Loan	22,00,000	
Current Liabilities	<u>11,00,000</u>	<u>33,00,000</u>
Net worth		<u>15,00,000</u>

Net worth = Share capital + Reserves = 15,00,000

$$\frac{\text{Capital}}{\text{Reserves and Surplus}} = \frac{1}{4} \Rightarrow \text{Share Capital} = 15,00,000 \times \frac{1}{5} = \text{Rs. } 3,00,000$$

$$\text{Reserves and Surplus} = 15,00,000 \times \frac{4}{5} = \text{Rs. } 12,00,000$$

Profit and Loss Account of PQR Ltd.
for the year ended 31st December, 2006

Particulars	Rs.	Particulars	Rs.
To Direct Materials	13,26,000	By Sales	78,00,000
To Direct Wages	6,63,000		
To Works (Overhead)	46,41,000		
Balancing figure			
To Gross Profit c/d (15% of Sales)	<u>11,70,000</u>		
	<u>78,00,000</u>		<u>78,00,000</u>
To Selling and Distribution Expenses (Balancing figure)	5,46,000	By Gross Profit b/d	11,70,000
To Net Profit (8% of Sales)	<u>6,24,000</u>		
	<u>11,70,000</u>		<u>11,70,000</u>

Balance Sheet of PQR Ltd.
as at 31st December, 2006

Liabilities	Rs.	Assets	Rs.
Share Capital	3,00,000	Fixed Assets	26,00,000
Reserves and Surplus	12,00,000	Current Assets:	
Long term loans	22,00,000	Stock of Raw Material	3,31,500
Current liabilities	11,00,000	Stock of Finished Goods	3,97,800
		Debtors	12,82,192
		Cash	<u>1,88,508</u>
	<u>48,00,000</u>		<u>48,00,000</u>

(b) Debt Securitisation

It is a method of recycling of funds. It is especially beneficial to financial intermediaries to support the lending volumes. Assets generating steady cash flows are packaged together and against this asset pool market securities can be issued.

The basic debt securitisation process can be classified in the following three functions:

- (i) The origination function: A borrower seeks a loan from a finance company, bank or a lease from a leasing company. The credit worthiness of the borrower is evaluated and a contract is entered into with repayment schedule over the life of the loan.
- (ii) The pooling function: Similar loans or receivables are clubbed together to create an underlying pool of assets. This pool is transferred in favour of a SPV – (Special Purpose Vehicle), which acts as a trustee for the investor.
- (iii) The securitisation function: It is the SPV's job now to structure and issue the securities on the basis of the asset pool. The securities carry a coupon and an expected maturity which can be asset based or mortgage based. These are generally sold to investors through merchant bankers.

Question 7

- (a) JKL Ltd. is considering the revision of its credit policy with a view to increasing its sales and profit. Currently all its sales are on credit and the customers are given one month's time to settle the dues. It has a contribution of 40% on sales and it can raise additional funds at a cost of 20% per annum. The marketing manager of the company has given the following options along with estimates for considerations:

Particulars	Current Position	I Option	II Option	III Option
Sales (Rs. in lakhs)	200	210	220	250
Credit period (in months)	1	1½	2	3

Bad debts (% of sales)	2	2½	3	5
Cost of Credit administration (Rs. in lakhs)	1.20	1.30	1.50	3.00

You are required to advise the company for the best option.

- (b) What do you mean by factoring? Describe the benefits of factoring.

(8 + 4 = 12 Marks)

Answer

- (a) Evaluation of the Different Options in Credit Policy of JKL Ltd.

(Rs. in lakhs)

Credit period	1 month Current position	1.5 months Option I	2 months Option II	3 months Option III
Sales	200	210	220	250
Contribution @ 40%	80	84	88	100
Increase in contribution over current level	—	4	8	20 (A)
Debtors = $\frac{\text{Average Collection Period} \times \text{Credit Sales}}{12}$	$\frac{1 \times 200}{12} = 16.67$	$\frac{1.5 \times 210}{12} = 26.25$	$\frac{2 \times 220}{12} = 36.67$	$\frac{3 \times 250}{12} = 62.50$
Increase in debtors over current level	—	9.58	20.00	45.83
Cost of funds for additional amount of debtors @ 20%	—	1.92	4.00	9.17 (B)
Credit administrative cost	1.20	1.30	1.50	3.00
Increase in credit administration cost over present level	—	0.10	0.30	1.80 (C)
Bad debts	4.00	5.25	6.60	12.50
Increase in bad debts over current levels	—	1.25	2.60	8.50 (D)
Net gain/loss A – (B + C + D)	—	0.73	1.10	0.53

Advise: It is suggested that the company JKL Ltd. should implement Option II which has a credit period of 2 months.

- (b) Factoring

Factoring involves provision of specialised services relating to credit investigation, sales ledger management, purchase and collection of debts, credit protection as well as provisions of finance against receivables and risk bearing. In factoring, accounts

receivables are generally sold to a financial institution that charges commission and bears the credit risks associated with it.

Thus, factoring is not just a single service, rather a portfolio of complimentary financial services available to clients i.e. sellers. The sellers are free to avail of any combination of services offered by the factoring organisations according to their individual requirements.

Benefits of Factoring

- (i) The firm can convert accounts receivables into cash without bothering about repayment.
- (ii) Factoring ensures a definite pattern of cash inflows.
- (iii) Continuous factoring virtually eliminates the need for credit department.
- (iv) Unlike an unsecured loan, compensating balances are not required in this case. Another advantage consists of relieving the borrowing firm of substantial credit and collection costs and to a degree from a considerable part of cash management.

Question 8

- (a) You are required to determine the weighted average cost of capital of a firm using (i) book-value weights and (ii) market value weights. The following information is available for your perusal:

Present book value of the firm's capital structure is:

	Rs.
Debentures of Rs. 100 each	8,00,000
Preference shares of Rs. 100 each	2,00,000
Equity shares of Rs. 10 each	<u>10,00,000</u>
	<u>20,00,000</u>

All these securities are traded in the capital markets. Recent prices are:

Debentures @ Rs. 110, Preference shares @ Rs. 120 and Equity shares @ Rs. 22.

Anticipated external financing opportunities are as follows:

- (i) Rs. 100 per debenture redeemable at par : 20 years maturity 8% coupon rate, 4% floatation costs, sale price Rs. 100.
- (ii) Rs. 100 preference share redeemable at par : 15 years maturity, 10% dividend rate, 5% floatation costs, sale price Rs. 100.
- (iii) Equity shares : Rs. 2 per share floatation costs, sale price Rs. 22.

In addition, the dividend expected on the equity share at the end of the year is Rs. 2 per share; the anticipated growth rate in dividends is 5% and the firm has the practice of paying all its earnings in the form of dividend. The corporate tax rate is 50%.

- (b) Explain briefly the propositions made in Modigliani and Miller approach on cost of capital.

(9 + 3 = 12 Marks)

Answer

- (a) Working Notes:

Determination of Specific Costs:

- (i) Cost of Debentures before tax (k_d)

$$k_d = \frac{I + \frac{(P - NP)}{n}}{\frac{(P + NP)}{2}}$$

Where,

I = Annual interest payment

P = Redeemable/payable value of debenture at maturity

NP = Net sale value from issue of debenture/face value – expenses

$$\begin{aligned} k_d &= \frac{8 + \frac{(100 - 96)}{20}}{\frac{(100 + 96)}{2}} \\ &= \frac{8 + .20}{98} = .0836 \text{ or } 8.36\% \end{aligned}$$

Cost of debenture after tax = $K_d (1 - t)$

$$= 8.36 (1 - .50) = 4.18\%.$$

- (ii) Cost of Preference Shares (k_p)

$$k_p = \frac{D + \frac{(P - NP)}{n}}{\frac{(P + NP)}{2}}$$

Where,

D = Fixed annual dividend

P = Redeemable value of preference shares

n = Number of years to maturity.

$$K_p = \frac{10 + \frac{(100 - 95)}{2}}{\frac{(100 + 95)}{2}}$$

$$= \frac{10.33}{97.5} = .1059 \text{ or } 10.59\%$$

(iii) Cost of Equity (k_e)

$$k_e = \frac{D}{NP} + g$$

Where,

D = Expected dividend per share

NP = Net proceeds per share

g = Growth expected in dividend

$$k_e = \frac{2}{22 - 2} + .05 = \frac{2}{20} + .05 = .10 + .05 = .15 \text{ or } 15\%.$$

(i) Computation of Weighted Average Cost of Capital based on Book Value Weights

Source of Capital	Book Value Rs.	Weights to Total Capital	Specific Cost	Total Cost
Debentures (Rs. 100 per debenture)	8,00,000	0.40	0.0418	0.0167
Preference Shares (Rs. 100 per share)	2,00,000	0.10	0.1059	0.0106
Equity Shares (Rs. 10 per share)	<u>10,00,000</u>	<u>0.50</u>	0.1500	<u>0.0750</u>
	<u>20,00,000</u>	<u>1.00</u>		<u>0.1023</u>

Cost of Capital = 10.23%

(ii) Computation of Weighted Average Cost of Capital based on Market Value Weights

Source of Capital	Market Value Rs.	Weights to Total Capital	Specific Cost	Total Cost
Debentures (Rs. 110 per debenture)	8,80,000	0.2651	0.0418	0.01108
Preference Shares (Rs. 120 per share)	2,40,000	0.0723	0.1059	0.00766
Equity Shares (Rs. 22 per share)	<u>22,00,000</u>	<u>0.6626</u>	0.1500	<u>0.09939</u>
	<u>33,20,000</u>	<u>1.00</u>		<u>0.11813</u>

Cost of Capital = 11.81%

(b) Propositions made by Modigliani and Miller on Cost of Capital

The propositions made by Modigliani and Miller on cost of capital are:

- (i) The total market value of a firm and its cost of capital are independent of its capital structure. The total market value of the firm is given by capitalising the expected stream of operating earnings at a discount rate considered appropriate for its risk class.
- (ii) The cost of equity (K_e) is equal to capitalisation rate of pure equity stream plus a premium for financial risk. The financial risk increases with more debt content in the capital structure. As a result, K_e increases in a manner to offset exactly the use of less expensive source of funds.
- (iii) The cut-off rate for investment purposes is completely independent of the way in which the investment is financed.

Question 9

- (a) A company is considering the proposal of taking up a new project which requires an investment of Rs. 400 lakh on machinery and other assets. The project is expected to yield the following earnings (before depreciation and taxes) over the next five years:

Year	Earnings (Rs. in lakh)
1	160
2	160
3	180
4	180
5	150

The cost of raising the additional capital is 12% and assets have to be depreciated at 20% on 'Written Down Value' basis. The scrap value at the end of the five years' period may be taken as zero. Income-tax applicable to the company is 50%.

You are required to calculate the net present value of the project and advise the management to take appropriate decision. Also calculate the Internal Rate of Return of the Project.

Note: Present value of Re. 1 at different rates of interest are as follows:

Year	10%	12%	14%	16%
1	0.91	0.89	0.88	0.86
2	0.83	0.80	0.77	0.74
3	0.75	0.71	0.67	0.64
4	0.68	0.64	0.59	0.55
5	0.62	0.57	0.52	0.48

- (b) State the differences between Global Depository Receipts and American Depository Receipts. (8 + 4 = 12 Marks)

Answer

- (a) (i) Calculation of Net Cash Flow

(Rs. in lakhs)

Year	Profit before dep. and tax	Depreciation (20% on WDV)	PBT	PAT	Net cash flow
(1)	(2)	(3)	(4)	(5)	(3) + (5)
1	160	$400 \times 20\% = 80$	80	40	120
2	160	$(400 - 80) \times 20\% = 64$	96	48	112
3	180	$(320 - 64) \times 20\% = 51.2$	128.8	64.4	115.6
4	180	$(256 - 51.2) \times 20\% = 40.96$	139.04	69.52	110.48
5	150	$(204.8 - 40.96) = 163.84^*$	-13.84	-6.92	156.92

*including depreciation and loss on disposal of assets.

- (ii) Calculation of Net Present Value (NPV)

(Rs. in lakhs)

Year	Net Cash Flow	12%		14%		16%	
		D.F	P.V	D.F	P.V	D.F	P.V
1	120	.89	106.8	.88	105.60	.86	103.2
2	112	.80	89.6	.77	86.24	.74	82.88
3	115.6	.71	82.08	.67	77.45	.64	73.98
4	110.48	.64	70.70	.59	65.18	.55	60.76
5	156.92	.57	<u>89.44</u>	.52	<u>81.60</u>	.48	<u>75.32</u>
			438.62		416.07		396.14
	Less: Initial Investment		400.00		<u>400.00</u>		<u>400.00</u>
	NPV		<u>38.62</u>		<u>16.07</u>		<u>-3.86</u>

- (iii) Advise: Since Net Present Value of the project at 12% = 38.62 lakhs, therefore the project should be implemented.

- (iv) Calculation of Internal Rate of Return (IRR)

$$IRR = 14\% + \frac{16.07 \times 2\%}{16.07 - (-3.86)}$$

$$\begin{aligned} &= 14\% + \frac{32.14}{19.93} \\ &= 14\% + 1.61\% = 15.61\%. \end{aligned}$$

(b) Global Depository Receipts and American Depository Receipts

Global Depository Receipts (GDR) are basically negotiable certificates denominated in US dollars, that represent a non-US company's publicly traded local currency equity shares. These are created when the local currency shares of Indian company are delivered to the depository's local custodian bank, against which the depository bank issues Depository Receipts in US dollars.

Whereas, American Depository Receipts (ADR) are securities offered by non-US companies who want to list on any of the US exchange. Each ADR represents a certain number of a company's regular shares. ADRs allow US investors to buy shares of these companies without the costs of investing directly in a foreign stock exchange. ADRs are issued by an approved New York bank or trust company against the deposit of the original shares. These are deposited in a custodial account in the US. Such receipts have to be issued in accordance with the provisions stipulated by the SEC USA which are very stringent.

The Indian companies have preferred the GDRs to ADRs because the US market exposes them to a higher level of responsibility than a European listing in the areas of disclosure, costs, liabilities and timing.

The Suggested Answers for Paper – 5: Income-tax and Central Sales Tax are based on the provisions applicable for A.Y.2007-08, which is the assessment year relevant for May 2007 examination.

PAPER – 5 : INCOME TAX AND CENTRAL SALES TAX

Answer all questions

Question 1

- (a) Dr. Sparsh Kumar is running a clinic. His Income and Expenditure account for the year ending 31st March, 2007 is given below:

Expenditure	Amount Rs.	Income	Amount Rs.
To Staff Salary	4,30,000	By Fees Receipts	12,63,600
To Consumables	9,250	By Dividend from Indian Companies	9,500
To Medicine consumed	3,64,800	By Winning from Lotteries Net of TDS (TDS Rs.12,240)	27,760
To Depreciation	91,000	By Income-tax refund	2,750
To Administrative Expenses	1,46,000		
To Donation to Prime Minister's Relief Fund	15,000		
To Excess of Income over expenditure	2,47,560		
Total	13,03,610	Total	13,03,610

- (i) Depreciation in respect of all assets has been ascertained at Rs.50,000 as per Income-tax Rules.
- (ii) Medicines consumed include medicine of (cost) Rs.16,000 used for his family.
- (iii) Fees Receipts include Rs.14,000 honorarium for valuing medical examination answer books.
- (iv) He has also received Rs.80,000 on account of Agricultural Income which had not been included in the above Income and Expenditure Account.
- (v) He has also received Rs.57,860 on maturity of one LIC Policy, not included in the above Income and Expenditure Account.
- (vi) He received Rs.6,000 per month as salary from a City Care Centre. This has not been included in the 'Fees Receipts' credited to Income and Expenditure Account.

(vii) He has sold land in June, 2006 for Rs.6,00,000 (valuation as per stamp valuation authority Rs.8,00,000). The land was acquired by him in October, 1998 for Rs.4,50,000.

(viii) He has paid premium of one LIC Policy Rs.12,000 (sum assured Rs.50,000).

(ix) He has paid Rs.2,500 for purchase of lottery tickets.

From the above compute the income and tax payable of Dr. Sparsh Kumar for the Asst. year 2007-08.

Cost Inflation Index: F.Y. 1998-99 – 351; F.Y. 2006-07 - 519. (20 Marks)

- (b) M/s Sidhant & Co., a sole proprietary concern is converted into a company, Sidhant Co. Ltd. with effect from November 29, 2006. The written down value of assets as on April 1, 2006 is as follows:

Items	Rate of Depreciation	WDV as on 1st April, 06
Building	10%	Rs.3,50,000
Furniture	10%	Rs.50,000
Plant and Machinery	15%	Rs.2,00,000

Further, on October 15, 2006, M/s Sidhant & Co. purchased a plant for Rs.1,00,000 (rate of depreciation 15%). After conversion, the company added another plant worth Rs.50,000 (rate of depreciation 15%).

Compute the depreciation available to (i) M/s Sidhant & Co. and (ii) Sidhant Co. Ltd. for Asst. year 2007-08. (10 Marks)

Answer

- (a) Computation of total income and tax liability of Dr. Sparsh Kumar for the A.Y. 2007-08

Particulars	Rs.
Income from salary (Working Note – 1)	72,000
Income from business (Working Note – 2)	2,65,550
Long-term capital gains (Working Note – 3)	1,34,615
Income from other sources (Working Note – 4)	54,000
Gross Total Income	5,26,165
Less: Deduction under Chapter VI-A (Working Note – 5)	25,000
Total Income	5,01,165
Tax on total income (Working Note - 6)	99,888
Add: Education cess @ 2%	1,998
Total tax liability	1,01,886
Less: Tax deducted at source (TDS)	12,240
Tax payable	89,646

Working Notes:

1. Computation of salary income

Particulars	Rs.
Gross Salary (6,000×12)	72,000
Less: Deduction under section 16	Nil
Net Salary	<u>72,000</u>

2. Computation of income under the head "Profits and gains of business or profession"

Particulars	Rs.	Rs.
Net Income as per Income and Expenditure Account		2,47,560
Add: Expenses disallowed:		
Depreciation (91,000 - 50,000)	41,000	
Cost of medicine for self-use	16,000	
Donation to Prime Minister's Relief Fund	15,000	72,000
		<u>3,19,560</u>
Less: Dividend from Indian companies	9,500	
Income-tax refund	2,750	
Winning from Lotteries	27,760	
Honorarium for valuing answer books	14,000	54,010
		<u>2,65,550</u>

3. Computation of Capital Gains

Particulars	Rs.	Rs.
Sale consideration	6,00,000	
Valuation as per Stamp Valuation Authority (Value to be taken higher of actual sale consideration or valuation adopted for stamp duty purposes as per section 50C)	8,00,000	
Consideration for the purpose of capital gain		8,00,000
Less:		
Cost of acquisition = $\frac{4,50,000 \times 519}{351}$		6,65,385
Long term capital gain		<u>1,34,615</u>

4. Computation of income under the head “Income from other sources”

Particulars	Rs.	Rs.
Dividend from Indian Companies [Exempt u/s 10(34)]		-
Honorarium for valuing answer books		14,000
Winning from Lotteries (Net)	27,760	
Add: TDS	12,240	40,000
Income from other sources		<u>54,000</u>

Note – As per section 58(4), no expense or deduction is allowable in respect of winnings from lotteries.

5. Computation of deduction under Chapter VI-A

Particulars	Rs.
U/s 80C Life Insurance Premium (maximum 20% of sum assured)	10,000
U/s 80G Donation to Prime Minister's Relief Fund [See Note below]	15,000
Total deduction under Chapter VI-A	<u>25,000</u>

Note – It is assumed that the donation is made to the Prime Minister's National Relief Fund and therefore, 100% deduction has been allowed under section 80G. It is also possible to compute the deduction under section 80G assuming that donation has been made to Prime Minister's Drought Relief Fund. In such a case, the exemption would be restricted to 50% of Rs.15,000. The calculation of total income and tax liability would accordingly change.

6. Computation of tax on total income

Particulars	Rs.
Tax on agricultural income plus non-agricultural income	
i.e. tax on Rs.5,81,165, being Rs.80,000 + 5,01,165 [See Note below]	1,10,888
Less: Tax on agricultural income plus basic exemption limit	
i.e. tax on Rs.1,80,000, being Rs.80,000 + 1,00,000	11,000
Tax on total income	<u>99,888</u>

Note - Tax on Rs.5,81,165 is computed hereunder -

Particulars	Rs.
Tax on long term capital gain	
Rs.1,34,615 @ 20%	26,923
Tax on winnings from lotteries	
Rs.40,000 @ 30%	12,000
Tax on balance income of Rs.4,06,550	<u>71,965</u>
	<u>1,10,888</u>

Note - Agricultural income is exempt from tax. It is considered for rate purpose only.

7. It is assumed that the sum received under a life insurance policy is one wholly exempt from tax under section 10(10D), fulfilling the conditions therein.
- (b) In the case of conversion of sole proprietary concern into a company as per section 47(xiv), the depreciation should be first calculated for the whole year assuming that no succession had taken place. Thereafter, the depreciation should be apportioned between the sole proprietary concern and the company in the ratio of the number of days for which the assets were used by them. It is assumed that in this case, the conditions specified in section 47(xiv) are satisfied and the assets have been used on all days.

Computation of depreciation allowable to Sidhant & Co. for A.Y.2007-08

Particulars	Rs.	Rs.
Building		
WDV as on 1.4.2006	3,50,000	
Depreciation@10%		35,000
Furniture		
WDV as on 1.4.2006	50,000	
Depreciation@10%		5,000
Plant and Machinery		
WDV as on 1.4.2006	2,00,000	
Add: Additions during the year (purchased on 15.10.06)	1,00,000	
	<u>3,00,000</u>	
Less: Depreciation for the year		
(15% of Rs.2,00,000 + 50% of 15% of Rs.1,00,000)		37,500
(Depreciation on new machinery is restricted to 50% of eligible depreciation, since the asset is put to use for less than 180 days in that year)		
Total depreciation for the year		<u>77,500</u>
Proportionate depreciation allowable to Sidhant & Co. for 242 days (i.e. 1.4.06 to 28.11.06) (i.e. $242/365 \times \text{Rs.}77,500$)		51,384

Computation of depreciation allowable to Sidhant Co. Ltd. for A.Y.2007-08

Particulars	Rs.
(i) Depreciation on the assets on conversion Proportionately for 123 days i.e. after conversion period $123/365 \times \text{Rs.}77,500$	26,116
(ii) Depreciation @ 50% of normal rate of 15% on Rs.50,000, being the value of plant purchased after conversion, which was put to use for less than 180 days	3,750
Depreciation allowable to Sidhant Co. Ltd.	<u>29,866</u>

Question 2 (First Alternative)

- (a) Explain marginal relief and calculate the amount of tax payable and amount of marginal relief availed on the income of Rs.10,30,000 by an individual for A.Y. 2007-08. (6 Marks)
- (b) List out the conditions for availing deduction under section 80QCB of Income-tax Act, 1961. (6 Marks)

Answer

- (a) In case of individuals/HUFs/AOPs/BOIs having a total income exceeding Rs.10,00,000, the additional amount of income-tax payable (together with surcharge) on the excess of income over Rs.10,00,000 should not be more than the amount of income exceeding Rs.10,00,000. This is called marginal relief.

In case an individual has a total income of Rs.10 lakhs, tax on his income would be = 10% of Rs.50,000 + 20% of Rs.1,00,000 + 30% of Rs.7,50,000 = Rs.2,50,000. Surcharge is not attracted on this tax since the total income does not exceed Rs.10 lakh.

However, if his total income is Rs.10,30,000, then tax on this income = 10% of Rs.50,000 + 20% of Rs.1,00,000 + 30% of Rs.7,80,000 = Rs.2,59,000

Add: Surcharge = Rs. 25,900 [10% of Rs.2,59,000]

Total tax plus surcharge = Rs.2,84,900

On comparing the two situations, it can be seen that for Rs.30,000 (i.e. Rs.10,30,000 – Rs.10,00,000) increase in the total income, the tax liability including surcharge has increased by Rs.34,900 (i.e. Rs.2,84,900 – 2,50,000). In such a case, the tax payable cannot exceed Rs.2,80,000, being Rs.2,50,000 + Rs.30,000.

Therefore, tax payable = Rs.2,50,000 + Rs.30,000 = Rs.2,80,000

Marginal relief = Rs.34,900 – Rs.30,000 = Rs.4,900

(b) Conditions for availing deduction under section 80QQB

- (i) Under section 80QQB, deduction upto a maximum of Rs.3,00,000 is allowed to an individual resident in India in respect of income derived as author. The deduction shall be the income derived as author or Rs.3,00,000, whichever is less.
- (ii) This income may be received either by way of a lumpsum consideration for the assignment or grant of any of his interests in the copyright of any book or by way of royalties or copyright fees (whether receivable in lump sum or otherwise) in respect of such book.
- (iii) Such book should be a work of literary, artistic or scientific nature.
- (iv) This deduction shall not be available in respect of royalty income from text book for schools, guides, commentaries, newspapers, journals, pamphlets and publication of similar nature.
- (v) For the purpose of calculating the deduction under this section, the amount of eligible income (before allowing expenses attributable to such income) shall not exceed 15% of the value of the books sold during the previous year. However, this condition is not applicable where the royalty or copyright fees is receivable in lump sum in lieu of all rights of the author in the book.
- (vi) For claiming the deduction, the assessee has to furnish a certificate in the prescribed form, duly verified by the person responsible for making such payment, setting forth such particulars as may be prescribed.
- (vii) Where the assessee earns any income from any source outside India, he should bring such income into India in convertible foreign exchange within a period of six months from the end of the previous year in which such income is earned or within such further period as the competent authority may allow in this behalf for the purpose of claiming deduction under this section.

Question 2 (Second Alternative)

- (a) Explain the provisions relating to multiplex theatres and convention centres under section 80-IB of the Income-tax Act, 1961. (6 Marks)
- (b) Discuss the tax implications arising consequent to conversion of a capital asset into stock-in-trade of business and its subsequent sale. (6 Marks)

Answer

- (a) "Multiplex theatre" means a building of a prescribed area, comprising of two or more cinema theatres and commercial shops of such size and number and having such other facilities and amenities as may be prescribed. Multiplex theatres located in cities other than Kolkata, Chennai, Delhi or Mumbai are eligible for tax incentive contained in section 80-IB(7A).

"Convention centre" means a building of a prescribed area comprising of convention halls to be used for the purpose of holding conferences and seminars being of such size and number and having such facilities and amenities as may be prescribed. Convention

centres situated in any place in India are eligible for tax incentive contained in section 80-IB(7B) on fulfillment of the conditions specified therein.

The following conditions have to be satisfied for availing the tax incentives under clauses (7A) & (7B) of section 80-IB -

- (i) The multiplex theatre / convention centre should be constructed at any time between 1.4.2002 and 31.03.2005.
- (ii) The business of the multiplex theatre / convention centre should not be formed by the splitting up, or the reconstruction, of a business already in existence or by the transfer of any building or machinery or plant previously used, to the new business.
- (iii) The assessee should furnish along with the return of income, an audit report from a chartered accountant in the prescribed form and manner certifying that the deduction has been correctly claimed.

Quantum of deduction: The amount of deduction shall be 50% of the profits from the business of building, owning and operating the multiplex theatre / convention centre. The deduction shall be available for 5 consecutive years beginning with the initial assessment year i.e. the assessment year relevant to the previous year in which -

- (i) a cinema hall, being a part of the multiplex theatre, starts operating on a commercial basis;
 - (ii) the convention centre starts operating on a commercial basis.
- (b) The conversion of a capital asset into stock-in-trade is treated as a transfer under section 2(47). It would be treated as a transfer in the year in which the capital asset is converted into stock-in-trade. However, as per section 45(2), the profits or gains arising from the transfer by way of conversion of capital assets into stock-in-trade will be chargeable to tax only in the year in which the stock-in-trade is sold. For the purpose of computing capital gains in such cases, the fair market value of the capital asset on the date on which it was converted into stock-in-trade shall be deemed to be the full value of consideration received or accruing as a result of the transfer of the capital asset.

On subsequent sale of such stock-in-trade, business profits would arise. The business income chargeable to tax would be the difference between the price at which the stock-in-trade is sold and the fair market value on the date of conversion of the capital asset into stock-in-trade.

Question 3

- (a) State with reasons in brief whether the following statements are true or false with reference to the provisions of the Income-tax Act, 1961:
- (i) Voluntary contributions received by charitable trusts, universities and educational institutions are not taxable as the definition of income in section 2(24) does not cover the same.
 - (ii) Surcharge payable by a foreign company on total income is 2.5% for A.Y. 2007-08.

- (iii) Income escaping assessment relating to assessment year 2004-05 is Rs.2,00,000. The time limit for issue of the notice under section 148 is 31st March, 2006.
- (iv) Mr. S is employed with T Ltd. as a Chartered Accountant. The annual membership fee of Mr. S paid by T Ltd. is not a perquisite and hence not chargeable to tax.
- (v) An assessee being aggrieved by the order of Assessing Officer can file a revision petition to the Commissioner of Income-tax within a period of two years.

(5 x 2 =10 Marks)

(b) Fill in the blanks with reference to the provisions of the Income-tax Act:

- (i) The maximum period for which speculation loss can be carried forward is years.
- (ii) M Ltd. gives a gift of Rs.7,500 to its employee Ganesh on his birthday. The taxable value of the gift in the hands of Ganesh is
- (iii) The exemption limit of income available to a senior citizen is Rs. for Asst. year 2007-08.
- (iv) The time limit for filing an appeal before Income-tax Appellate Tribunal is days of the receipt of appeal order from Commissioner of Income-tax (Appeals).
- (v) Mr. Z has paid a sum of Rs.65,000 on 30.11.2006 as tuition fees to a university in Australia. The amount deductible under section 80C for A.Y. 2007-08 is Rs.....

(1 x 5 = 5 Marks)

Answer

- (a) (i) False - Section 2(24) defining the term 'income' includes voluntary contributions received by any trust, university or educational institution. Hence, the statement is not correct.
- (ii) True - Foreign companies have to pay 2.5% as surcharge on tax payable for A.Y.2007-08 as per Part III of the First Schedule to the Finance Act, 2006.
Note - Alternatively, it can be answered that the statement is false since surcharge @ 2.5% is calculated on tax payable and not on total income.
- (iii) False - As per section 149(1)(b), where the income escaping the assessment is Rs.1,00,000 or more, the time limit for issue of notice under section 148 is 6 years from the end of the relevant assessment year in which the income has escaped assessment.
- (iv) False - The membership fee payable to the Institute is an obligation of Mr. S, which is paid by his employer i.e. T Ltd. Under the definition of perquisite, an obligation of the employee paid off by the employer is treated as a perquisite and is hence chargeable to tax.
- (v) False - Under section 264 of the Income-tax Act, the assessee should file a revision petition within a period of one year.

- (b) (i) 4
- (ii) Nil
- (iii) 1,85,000
- (iv) 60
- (v) Nil

Question 4

Write short notes on any three of the following:

- (a) Deduction to be allowed on actual payment basis (Section 43B)
- (b) Scheme of submission of return through Tax Return Preparer (Section 139B)
- (c) Deduction from Gross Total Income under section 80GG
- (d) Incentives for newly established units in Special Economic Zone (Section 10AA).

(6 x 3 = 18 Marks)

Answer

- (a) Deductions to be allowed on actual payment basis (Section 43B)

The following sums are allowed as deduction only on the basis of actual payment within the time limit specified in section 43B, irrespective of the method of accounting followed by the assessee -

- (i) Any sum payable by way of tax, duty, cess or fee, by whatever name called, under any law for the time being in force.
- (ii) Any sum payable by the assessee as an employer by way of contribution to any provident fund or superannuation fund or gratuity fund or any other fund for the welfare of employees.
- (iii) Any sum paid to an employee as bonus or commission for services rendered.
- (iv) Any sum payable by the assessee as interest on any loan or borrowing from any public financial institution or a State Financial Corporation or a State Industrial Investment Corporation.
- (v) Any sum payable by the assessee as interest on any loan or advance from a scheduled bank.
- (vi) Any sum payable by the assessee as an employer in lieu of any leave at the credit of his employee.

The above sums should be paid by the assessee on or before the due date for furnishing the return of income under section 139(1), for the purpose of claiming deduction in the previous year in which the liability to pay such sum was incurred and the evidence of such payment should be furnished by the assessee along with such return. If the payment is made after the due date for filing the return, deduction can be claimed only in the year of actual payment.

- (b) Scheme of submission of return through Tax Return Preparer (Section 139B)
- (i) A new section 139B has been inserted with effect from June 1, 2006 so as to provide 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 authorized.
 - (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.
- (c) Deduction from Gross Total Income under section 80GG
- In order to claim deduction under section 80GG, the assessee should fulfill the following conditions:
- (i) He should be an individual, who pays rent for his residential accommodation.
 - (ii) He should not be in receipt of any house rent allowance

- (iii) He or his spouse or his minor child or HUF of which he is a member should not own any residential house at the place where he ordinarily resides or at the place of his business or employment.
- (iv) No claim for self-occupied property should be made in respect of any accommodation.
- (v) The assessee should file a declaration in Form No.10BA wherein he confirms the details of rent paid and fulfillment of the other conditions (Rule 11B).

The amount of deduction available to the assessee is restricted to the least of the following:

- (i) Rs.2,000 per month
- (ii) 25% of total income
- (iii) Excess of rent paid over 10% of total income.

Total income, for this purpose, means gross total income as reduced by all deductions under Chapter VIA except section 80GG.

- (d) Incentives for newly established units in Special Economic Zone [Section 10AA]
 - (i) This section applies to any undertaking, being the Unit, which has begun or begins to manufacture or produce articles or things or provide any services during the previous year relevant to the assessment year commencing on or after 1st April, 2006 in any Special Economic Zone (SEZ).
 - (ii) It provides for a tax holiday in computing the total income of an assessee, being an entrepreneur, from his Unit set up in a SEZ.
 - (iii) Such assessee should be an entrepreneur referred to in section 2(j) of the SEZ Act, 2005 i.e., a person who has been granted a letter of approval by the Development Commissioner under section 15(9).
 - (iv) Sub-section (1) provides for the quantum of deduction under this section, which is
 - (1) 100% of profits and gains derived from the export of such articles or things or from services for a period of 5 consecutive assessment years beginning with the assessment year relevant to the previous year in which the Unit begins to manufacture or produce such articles or things or provide services, as the case may be, and
 - (2) 50% of such profits and gains for further 5 assessment years and
 - (3) Thereafter, for the next 5 consecutive assessment years, so much of the amount not exceeding 50% of the profit as is debited to the profit and loss account of the previous year in respect of which the deduction is to be allowed and credited to a reserve account (to be called the "Special Economic Zone Reinvestment Reserve Account") to be created and utilised for the purposes of the business of the assessee in the prescribed manner.
 - (v) The profits derived from the export of articles or things or services (including computer software) shall be the amount which bears to the profits of the business of

the undertaking, being the Unit, the same proportion as the export turnover in respect of such articles or things or services bears to the total turnover of the business carried on by the assessee.

- (vi) The profits and gains derived from on site development of computer software (including services for development of software) outside India shall be deemed to be the profits and gains derived from the export of computer software outside India.

Question 5

- (a) State with brief reasons whether the following statements are true/false in the light of Central Sales-tax Act:

- (i) Hides and skins are declared goods. .
- (ii) Subsidy given by Government to manufacturers to compensate cost of production will form part of sale price.
- (iii) Packing charges realised by the dealer is an integral part of sale price.
- (iv) There is no time limit prescribed for liquidator on his assumption of charge for intimation to sales-tax authorities.
- (v) When goods are sent by VPP, the sale is said to take place in the State from where the parcel is sent. (2 x 5 = 10 Marks)

- (b) Fill in the blanks in the light of the provisions of Central Sales-tax Act:

- (i) Hari of Chennai made a sale of goods to an Export House in Delhi. These goods were later exported by the Export House to Canada. To enable Hari to claim the exemption under CST Act, the Export House should provide to Hari
- (ii) One of the essential features of an inter-State sale is that a transaction should be.....
- (iii) Vikas effected the first inter-State sale on 22.3.2007 and applied for registration on 20.4.2007. The effective date for registration will be
- (iv) Charity or Dharmada collected by the dealer.....form part of sale price.
- (v) The authority to declare goods of special importance lies with

(1x 5 = 5 Marks)

Answer

- (a) (i) True - Hides and Skins, whether in a raw or dressed state, are declared goods as per section 2(c) read with section 14.
- (ii) False - Government subsidy does not constitute amount payable to the dealer (by his customer) as consideration for the sale of goods. Hence, it is not includible in sale price.
- (iii) True - According to section 2(h), Sale Price includes any sum charged for anything done by the dealer in respect of the goods at the time of or before the delivery

thereof. Packing has been done before delivery and is hence includible. Packing charges realised by the dealer constitute an integral part of the sale price.

- (iv) False - The liquidator must give a notice of his having assumed charge to the appropriate authority within thirty days after he has become such liquidator.
 - (v) False – The sale transaction is complete only when the buyer/consignee accepts the VPP, since in the case of a sale by VPP, the property in the goods is passed at the time of payment of the price of the goods by the buyer and not before that. Hence, sale is said to take place in the State where goods are accepted and delivered.
- (b) (i) Form H
- (ii) a completed sale of goods/the cause of movement of goods from one State to another / effected by transfer of documents of title to the goods during their movement from one State to another.
- (iii) 22.3.2007
- (iv) Will / shall
- (v) Parliament / Central Government

Question 6

Explain any two of the following with reference to the provisions of the Central Sales-tax Act:

- (a) Act or omission for which penalties can be levied.
- (b) On what consideration goods of special importance are selected?
- (c) What are the relevant provisions under Central Sales-tax for forfeiture of security by the authority granting certificate of registration? (5 x 2 = 10 Marks)

Answer

- (a) Penalties can be levied under the Central Sales Tax Act for the following acts/omissions -

- (i) Furnishing a false certificate or declaration under section 6(2), 6A(1), 8(4) or 8(8), which he knows or has reason to believe to be false.

Section	Particulars	Form
6(2)	Transit sale	E I / E II Form
6A(1)	Consignment	F Form
8(4)	Inter-State sale	C Form / D Form
8(8)	Sale to Special Economic Zone	Prescribed form

- (ii) Failure to get registration or failure to furnish security as required under section 7.
- (iii) False representation by a registered dealer that goods purchased by him are covered by his certificate of registration.

- (iv) False representation by a dealer, who is not registered, that he is a registered dealer.
- (v) Failure without reasonable cause, by a dealer who has purchased goods for any of the purposes specified in section 8(3) or section 8(6), to make use of the goods for any such purpose.
- (vi) Possession of any form prescribed for the purpose of section 8(4) or section 8(8), but not obtained in accordance with the provisions of Act or Rules.
- (vii) Collection of taxes by an unregistered dealer or by a registered dealer in violation of the provisions of the Act or Rules.

Note – Any five of the above may be given in the answer.

- (b) Goods of special importance covered by section 14 are selected based on the following considerations, -
 - (1) It should be raw material or largely in the nature of raw material.
 - (2) Such raw material or finished goods made based on such raw material should, in terms of volume of inter-State transaction, be of special importance in inter-State trade or commerce and
 - (3) Such goods should be of special importance for the country as a whole, from the stand point of the consumer or of industry.
- (c) The security, either in whole or in part, can be forfeited by the authority granting the certificate of registration -
 - (i) for realising any amount of tax or penalty payable by the dealer; or
 - (ii) misuse of the forms (E I, E II, C, F) by the dealer; or
 - (iii) Failure by the dealer to keep the forms in proper custody.

Before any such order of forfeiture is passed, the dealer shall be given an opportunity of being heard. On account of any such order passed if the security is rendered insufficient, the dealer shall make up the deficiency, in such manner and within such time as may be prescribed by the concerned authority.

PAPER – 6 : INFORMATION TECHNOLOGY

Question No. 1 is compulsory.

Answer any four questions from remaining six questions.

Question 1

- (a) Convert the following from one number system to another system alongwith the Working Notes:

- (i) $(3CB.98)_{16} = (\quad)_2$
- (ii) $(AF.16C)_{16} = (\quad)_8$
- (iii) $(111.12)_8 = (\quad)_2$
- (iv) $(10101010.101)_2 = (\quad)_{10}$
- (v) $(123.15)_{10} = (\quad)_{16}$

- (b) Describe briefly, the following terms with reference to Information Technology:

- (i) FTP
- (ii) DBMS
- (iii) Duplex Printing
- (iv) Gateways
- (v) Asymmetric Crypto System.

- (c) Give one or two reasons for each of the following:

- (i) Use of Firewall in the system
- (ii) Need of Macro in spread sheet
- (iii) Use of USB port
- (iv) Use of Router
- (v) Use of Multiplexer.

- (d) Write True or False for each of the following statements:

- (i) Network database structure can be used to answer ad hoc queries.
- (ii) Computer Output Microfilm (COM) is Input as well as Output device.
- (iii) One GB represents 10,48,567 bytes.
- (iv) Laser printers speed is measured in PPM.
- (v) Screen resolution is measured in terms of Picture elements.

(5 + 5 + 5 + 5 = 20 Marks)

Answer

(a) (i) $(1111001011.10011000)_2$

(ii) $(257.0554)_8$

(iii) $(1001001.00101)_2$

(iv) $(170.625)_{10}$

(v) $(7B.26)_{16}$

Working of the above answers is given below:

(i) $(3\text{ CB.98})_{16} = (\quad)_2$

To convert the given number from Hexadecimal Number System to Binary Number System, each digit of the number will be represented in Binary form using a group of four bits. Adding or removing leading zeros if required.

$$(3\text{ CB.98}) = 0011\ 1100\ 1011\ 1001\ 1000$$

$$\text{Hence, } (3\text{ CB.98})_{16} = (11\ 11001011.10011000)_2$$

(ii) $(\text{AF.16 C})_{16} = (\quad)_8$

To convert the given number from Hexadecimal Number System to Octal Number System, each digit of the number will be represented in Binary form using a group of three bits. Adding or removing leading zeros if required.

$$\begin{aligned} (\text{AF.16 C}) &= 1010\ 1111\ 0001\ 0110\ 1100 \\ &= 010\ 101\ 111\ 000\ 101\ 101\ 100 \\ &= 2\ 5\ 7\ 0\ 5\ 5\ 4 \end{aligned}$$

$$\text{Hence, } (\text{AF.16 C})_{16} = (257.0554)_8$$

(iii) $(111.12)_8 = (\quad)_2$

To convert the given number from Octal Number System to Binary Number System, each digit of the number will be represented in Binary form using a group of three bits. Adding or removing leading zeros if required.

$$(111.12) = 001\ 001\ 001\ 001\ 010$$

$$\text{Hence, } (111.12)_8 = (1001001.00101)_2$$

(iv) $(10101010.101)_2 = (\quad)_{10}$

$$= 2^7 \times 1 + 2^6 \times 0 + 2^5 \times 1 + 2^4 \times 0 + 2^3 \times 1 + 2^2 \times 0 + 2^1 \times 1 + 2^0 \times 0 + 2^{-1} \times 1 + 2^{-2} \times 0 + 2^{-3} \times 1$$

$$= 128 + 0 + 32 + 0 + 8 + 0 + 2 + 0 + \frac{1}{2} + \frac{0}{4} + \frac{1}{8}$$

$$\text{Hence, } (10101010.101)_2 = (170.625)_{10}$$

(v) $(123.15)_{10} = (\quad)_{16}$

Step I

16	123	Remainder	
16	7	11	= B
	0	7	= 7

Step II

$$.15 \times 16 = 2.40 \rightarrow 2$$

$$.40 \times 16 = 6.40 \rightarrow 6$$

Hence,

$$(123.15)_{10} = (7B.26)_{16}$$

- (b) (i) FTP: It stands for File Transfer Protocol. It is used to upload the files from client computer to remote Web-server.
- (ii) DBMS: It is a complex system software package which allows the user to create and maintain the database files. Data security is defined with the help of DBMS using passwords and access rights. DBMS allows only authorized users to access the data according to their access privileges.
- (iii) Duplex Printing: Printing on both sides of a paper at the same time is called Duplex Printing.
- (iv) Gateways: It is used to connect two dissimilar networks but do not possess network management facilities. They are used to connect LANs of different topologies e.g. Bus and Ring Network.
- (v) Asymmetric Crypto System: In this cryptography technique, both the parties use different keys for encryption/decryption. The key known to the sender is called Private key and receiver key is called Public key. A person using asymmetric crypto system publishes his Public key so that it can be known to all the persons who want to confirm the identity of the sender.
- (c) (i) Use of Firewall in the system: Firewalls are systems that control the flow of traffic between the Internet and organisation's Local Area Network and Systems. Firewalls are packaged as turnkey hardware and software packages and are setup to enforce specific security policies that are desired. Firewall is an effective means of protecting the internal resources from unwanted intrusion.
- (ii) Need for Macro in Spreadsheet: Macro is a small programme that carries out predefined and prerecorded series of steps by giving a few keyboard shortcuts. We can say that Macro is like a recorded movie, which can be run any number of times. Macro is just a way of doing work in a series of steps, which it carries out

automatically once it is triggered. Hence, the need of Macro is to automate the tasks, thus saving lot of precious time.

- (iii) Use of USB port: USB stands for Universal Serial Bus. These ports provide the user with higher data transfer speeds for different USB devices like keyboard, mouse, scanners or digital camera.
 - (iv) Use of Router: Router is a special purpose computer or software package that handles the connection between two or more networks. Routers spend all their time looking at the destination addresses of the packets passing through them and deciding on which route the packets should be sent.
 - (v) Use of Multiplexer: This is a device that enables several devices to share one communication line. It scans each device to collect data for transmission on a single communication line. It is often used with a complementary demultiplexer on the receiving end. As such it restricts the need of multiple communication lines.
- (d) (i) False
 (ii) False
 (iii) False
 (iv) True
 (v) True

Question 2

Distinguish between the following:

- (i) Master file and Transaction file
- (ii) Logical record and Physical record
- (iii) Audio conferencing and Video conferencing
- (iv) Sequential file organization and Direct file organization
- (v) Client-server model and Peer to Peer model.

(4 × 5 = 20 Marks)

Answer

(i)	No.	Master File	Transaction File
	1.	This file stores the permanent records of an organization which show the current status.	This file stores daily transactions of an organization.
	2.	This file consists of static data and is less volatile in nature.	This file is frequently changed to store current transaction i.e. this file is highly volatile.
	3.	Master file is updated on the basis of transaction file.	Transaction file is used to update Master file.

4.	It is necessary to take the backup of Master files for security purpose.	Transaction files are no longer required after updation and transaction entries can be deleted after updation. Therefore, it is not essential to take the backup of these files.
5.	Records in master file are stored in ascending order of primary key.	Transaction file stores the entries in the order in which they arrive.
6.	Master file stores one record corresponding to each primary key.	There can be more than one entry for a particular master record.
7.	Examples of Master files are Item file, Customer file, Employee file etc.	Sales file, Day Book, deductions file etc. are examples of transaction files.

(ii)	No.	Logical Record	Physical Record
	1.	The record defined by user is called Logical Record.	Storage of Logical Record in the computer is called Physical Record.
	2.	It is the collection of those fields which are accessed by a single primary key.	It is the collection of those fields which are stored in adjacent memory location.
	3.	Logical records are linked together with the help of File pointers.	Physical records are linked together with the help of Address Pointers.
	4.	It may consist of Fixed length fields and Variable length fields.	All fixed length fields of Logical record are stored in one Physical record and each variable length field of Logical record is considered as separate physical record.
	5.	Field Names, their data type and width are defined by user according to the requirements.	Physical record size is defined by Database Administrator (DBA) in such a way that it results in faster accessing of data.
	6.	User is concerned with Logical record for insertion, deletion and updation of data.	Computer performs the required manipulation in the physical record.
	7.	Sequence of fields in Logical record may be according to the convenience of user.	Sequence of fields in Physical record may not be same as Logical record.

- (iii) **Audio Conferencing:** It is the use of audio communication equipments which allow the user to communicate with geographically dispersed persons. Audio conferencing does not require a computer but requires a two way audio communication facility.

Guidelines to make Audio conferencing more efficient are as stated below:

- (a) All the participants must have an opportunity to speak.
- (b) Number of participants must be kept to manageable size.
- (c) Copy of conferencing agenda must be sent to all the participants in advance through FAX.
- (d) Participants must identify themselves.
- (e) Conferencing discussion must be recorded.
- (f) Hard copy of the discussion must be prepared and should be sent to all the participants for approval.

Video Conferencing: It is the use of television equipment which allow the user to communicate with geographically dispersed persons. The equipment provides both sound and picture. The participant can see and hear each other and it does not required computers. Participants gather in specially equipped rooms having audio and video facility.

There are three types of Video Conferencing:

- (a) One way Video and Audio: In this case, audio and video is traveled only in one direction e.g. Television.
- (b) One way Video and Two way Audio: In this case, audio is transferred in both directions but video is transferred in one direction e.g. Discussion of News Reader with field correspondent.
- (c) Two way Video and Audio: In this case, audio and video is transferred in both directions between sender and receiver e.g. Discussion of persons between different studios of a News Channel.

(iv)	No.	Sequential File Organisation	Direct File Organisation
	1.	There exists a definite relationship among adjacent records.	No relationship exists among adjacent records, as records are stored randomly.
	2.	Desired record is searched by sequential access. Hence, more time is required to find the desired record.	Desired record is accessed by direct access, hence desired record is searched quickly.
	3.	Updation of Master file on the basis of Transaction file takes place by Brought-forward Carried-forward file method, in which original master file is retained.	Updation of Master file on the basis of Transaction file takes place by Overlaying in disk, in which original master file is overwritten by updated master records.
	4.	Tape devices support sequential file organization.	Direct Access Storage Devices (DASD) like Magnetic disk, Floppy disk, Optical

	organization.	Laser disk support Direct File Organisation.
5.	This file organization is suitable for batch processing like payroll application and is not used for on-line queries like Banking System, Railway/Airlines Reservation system.	This file organization is suitable for on-line applications like Banking System, Railway/Airlines Reservation System where immediate response is required.

(v)	No.	Client-Server model	Peer-to-Peer model
	1.	In this model, number of computers, known as clients are connected to a single host computer known as server.	In this model, all the computers are interconnected with each other. There is no concept of server and clients. All computers behave as server as well as clients.
	2.	It uses a dedicated server which provides various services to clients like hardware, software and data access. Different types of servers can be File, Fax, Print or Database server.	It uses non-dedicated server. Non-dedicated server can also be used as a node for data entry, processing and output operations.
	3.	Clients can share disk storage and printers attached with the server.	All computers can share the data/resources of each other.
	4.	It is suitable for large organization having large number of nodes.	It is suitable in small organisation having less number of nodes upto ten.
	5.	Data transfer speed is more.	Data transfer speed is less which decreases even further with the increase in number of computers.
	6.	Failure of server results in break-down of entire network.	Failure of one computer will not affect the working of other, only the data stored on the faulty computer will not be accessible to other computers.
	7.	Server can not be used for data entry/result purposes, hence it can be said that all the computers are not fully employed.	All the computers are fully employed.
	8.	Clients are required to be connected with server in a particular structure like Star Network.	Computers can be connected at any convenient point in the network like Ring Network.
	9.	Clients can be dumb terminal or	All computers are intelligent terminals.

	Intelligent terminals.	
10.	This architecture is employed where data security is of prime importance.	This architecture is used when security is not a bigger issue.

Question 3

- (a) Explain in brief, the floppy disk as an auxiliary device.
- (b) What is database structure? Explain relational database structure.
- (c) A company offers discounts to customers on the following basis:

Quantity ordered	Normal discount
Less than 101	5%
From 101 to 500	10%
From 501 to 1,000	15%
More than 1,000	20%

The normal discount as given above is admissible only if the Customer's account balance is below Rs. 1,000 and the order value is Rs. 10,000 or more. If the account does not satisfy both of these conditions, the discount is reduced by 2% and if only one condition is violated, the discount is reduced by 1%.

Draw a Flow Chart to print customer name, discount offered and net amount payable for 25 customers. (5 + 5 + 10 = 20 Marks)

Answer

- (a) Floppy Disk (Diskette): It consists of a circular plate, known as platter made of mylar plastic and coated with magnetic material like Ferrous Oxide on both the surfaces. The platter is enclosed in a protective jacket to avoid scratching on the magnetic surface. The circular plate is divided into number of concentric circles, known as tracks. Each track is divided into number of equal parts, known as sectors. Although different tracks vary in sizes but the volume of data stored on each track is same because the packing density of data goes on increasing as we move from outer to inner tracks. Outer track is called track 0. Any location on the floppy disk i.e. Physical address is identified by Surface number, Track number and Sector number.

Data recorded on the floppy disk is read with the help of a device, known as Floppy Disk Drive (FDD). There are two types of floppies – 5.25" (1.2 MB) and 3.5" (1.44 MB). In both cases, FDD required to read/write the data on floppy disks is different. Sony, IBM, Imation are the reputed manufacturers of floppy disks.

Different portions of the floppy disks are explained below:

- (i) Spindle hole: This hole is used to rotate the circular plate at very high speed, usually at the speed of 300 RPM (Rotations/revolutions per minute). Due to the movement of circular plate, each sector of a track comes under the R/W head of FDD.
 - (ii) Read/Write Access position: This is the position where R/W head of FDD touches the magnetic surface for the purpose of reading/writing. Initially, R/W head is adjusted on the outermost track i.e. track 0 and when this track is completely read or written, then R/W head moves horizontally to adjust itself on the next inner track i.e. Track 1 and so on.
 - (iii) Index Hole: It is used as a marker of first sector. If an imaginary line passing through the center of spindle hole and Index hole is drawn, then the sector starting from this line in the clockwise direction is called first sector.
 - (iv) Write protect button: It is used to write-protect the floppy. If floppy is write protected, then nothing can be written on the floppy but contents already stored on the floppy disk can be read.
- (b) The approach used to organize records and their relationships logically, is called Database Structure.

The three traditional data base structures are:

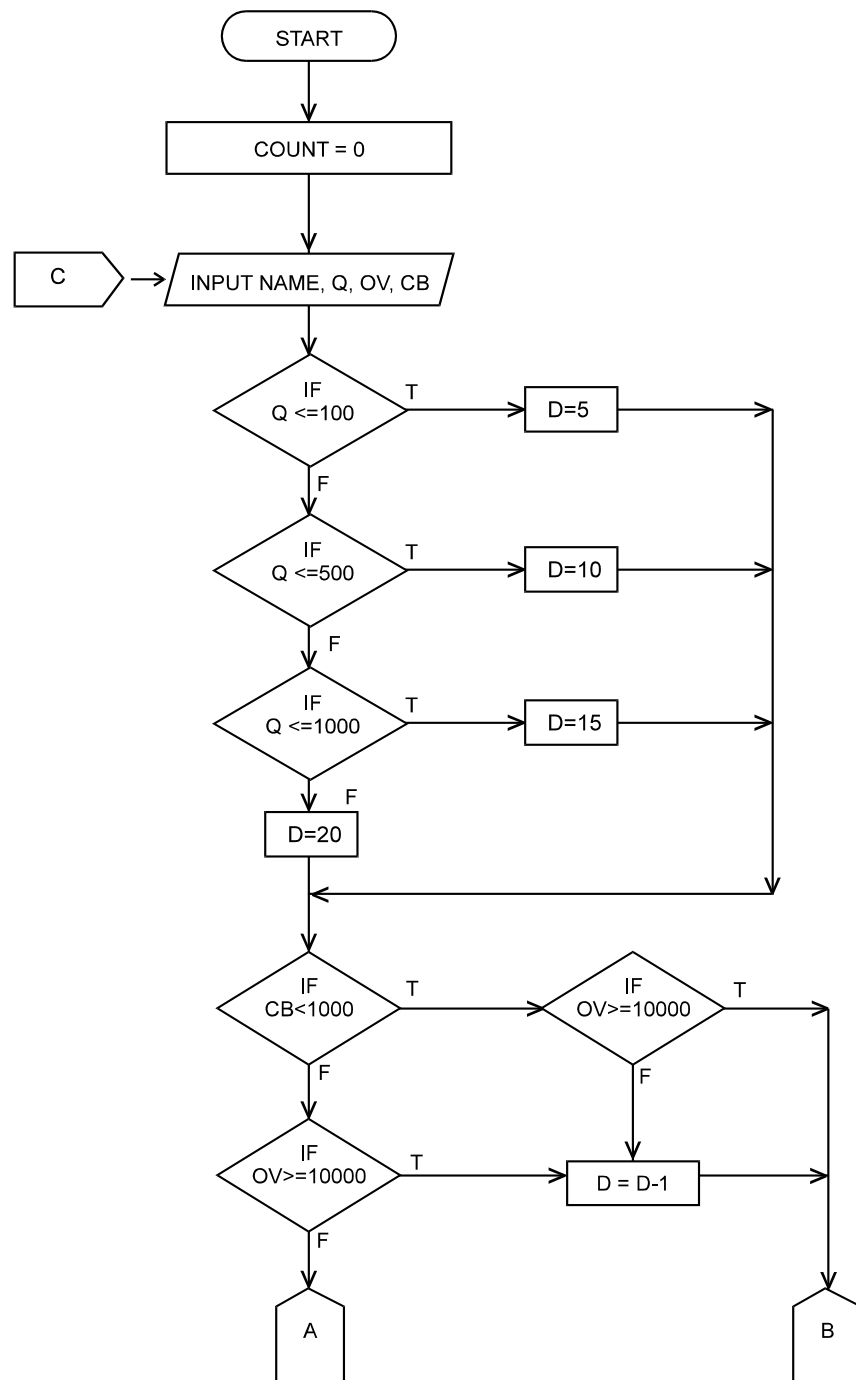
- (i) Hierarchical database structure.
- (ii) Network database structure.
- (iii) Relational database structure.

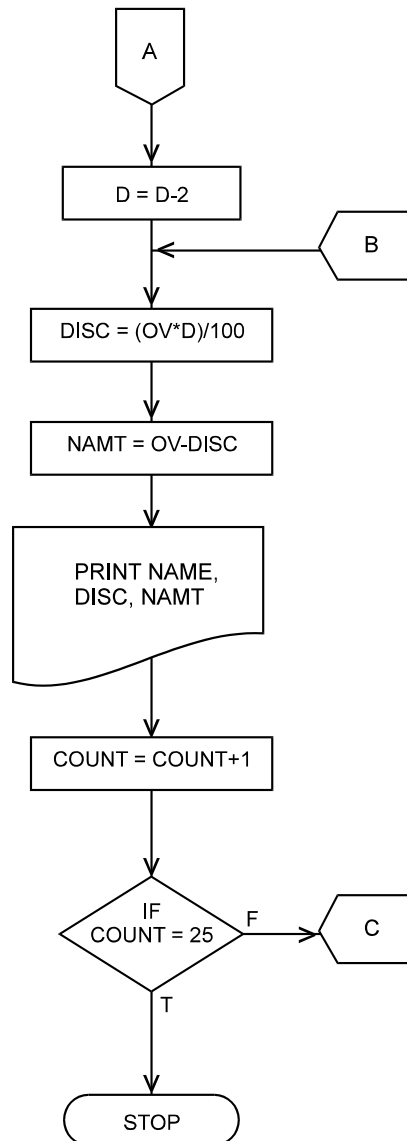
Relational database structure: In this database structures, records are stored in the form of two dimensional tables. The table is a file, in which each row represents one record and each column represents a field. In this database structure, relationships between the records need not to be specified in advance. Relational databases provide the flexibility in performing database queries and creating reports from more than one file by establishing the relationship among them on the basis of primary key. This relationship among the files can be created at any time according to the requirement and need not to be specified at the time of creation of database files.

The relational database structure is more flexible than hierarchical or network database structures in providing answers of ad hoc reports but it does not process the large batch applications with the speed of hierarchical or network databases. Examples of Relational Database Management Systems (RDBMS) include Oracle, IBM DB2, SQL Server, MS-Access etc.

- (c) Flowchart

The following Flow chart is on the next page.





Abbreviations:

Q	=	Quantity
OV	=	Order Value
CB	=	Customer's Accounts Balance
NAMT	=	Net Amount
D	=	Disscount

Disc = Discount offered

True = T

False = F

Question 4

- (a) Explain briefly various language tools available in MS-Word.
- (b) Define an operating system and explain various functions performed by it.
- (c) What are the integrity controls that DBMS package may offer? Explain in brief.

(5 + 5 + 10 = 20 Marks)

Answer

- (a) MS-Word offers following useful language tools to aid writing and to increase efficiency:
 - (i) Auto Correct: Auto correct has a dictionary of its own which contains a list of commonly mistyped words. Adding words we mistype, one can customize this dictionary. Correct spellings of the word is to be provided with which MS-Word should replace the mistyped word. Once the entry in the Auto Correct dictionary is made, word automatically makes corrections of such words. This saves the trouble of going back to make corrections every time the word is mistyped.
 - (ii) Auto Text: This is a unique feature of the word. It allows storing formatted text even paragraphs and graphics. These can be recalled by pressing some keys. Auto Text is like auto correct in that it also has dictionary of its own and can be customized. Auto text has an Auto complete tip that will complete the text without you having to type the entire word. New Auto text entries can be made for any text in the document using the Create Auto Text entry dialog box.
 - (iii) Spelling and Grammar: The spell checking function checks each word in the article against the dictionary and underlines it with a red curly line if the word with wrong spelling appears. Words not found in the dictionary are also marked with a red curly line. User on running the spell check function will be able to get the right spelling and rectify it. Additional words can also be added to the dictionary.
 - (iv) Thesaurus: Thesaurus is a book in which words and phrases of similar meaning are grouped together. It comes with Word package. With the help of Thesaurus, one can select the more precise word.
 - (v) Find and Replace Text: 'Find' command helps to locate specific text in a document while 'Replace' command helps to substitute it with new text. This has the option of replacing all found words with one keystroke if one is sure that all the entries of that word need to be replaced.
- (b) Operating systems are devised to optimize the man machine capabilities. An operating system is defined as an integrated system of programs, which supervises the operation of CPU, controls the input/output functions of computer system and provides various supports services. Without loading the operating system into the memory of the computer

system, the computer cannot be used. There are six basic functions that an operating system can perform.

- (i) Job scheduling: Operating system decides the sequence in which different jobs are executed, using priorities established by the organizations.
 - (ii) Manage hardware and software resources: Operating system helps in loading the application programme into the primary memory and helps the various hardware units to perform as specified in the application programme.
 - (iii) Maintain system security: Operating system identifies the authorized users by recognizing the password entered by the user and thereby authorizing the user to have access to the system.
 - (iv) Enable multiple users resource sharing: Operating system can handle the scheduling and execution of the application programmes for many users at the same time (Multi programming).
 - (v) Handle interrupts: An interrupt is a technique used by the operating system to temporarily suspend the processing of the programme in order to allow other programmes to be executed. Interrupts are issued when a programme requests an operation that does not require the CPU i.e., input/output devices or when the programme exceeds the pre-defined time limit.
 - (vi) Maintains usage records: Operating system can keep track of the amount of the time used by each user for each resource – processor, memory, Input/Output devices. Such information is usually maintained for the purpose of charging for the use of computing resources.
- (c) Data Integrity Controls (i.e. controls on the possible value a field can assume) can be built into the physical structure of the fields. In order to have the correct database, DBMS needs to have certain controls on the data fields. Some of the security controls that DBMS imposes on data fields are as follows:
- (i) Data Type: In the data field, the data type defines the type of data to be entered in the field. It may be numeric, character etc.
 - (ii) Length of data field: The length of data field defines the maximum number of characters or digits (depending upon the data type) to be entered in the data field. It may be 256, 65536 etc.
 - (iii) Default value: It is the value a field will assume unless a user enters an explicit value for an instance of that field. Assigning a default value to a field can reduce data entry time and entry of a value to that field can be skipped. Default value helps in reducing the probability of data entry errors for most common values.
 - (iv) Range Control: This limits the set of permissible values a field can assume. The range may be numeric lower to upper bound or a set of specific values. Range control must be used with caution since the limits of range may change with time. A combination of range control and coding led to Y2K problem, in which a field for the year was represented by only the numbers 00 to 99.

- (v) Null Value Control: Null value is an empty value. Each primary key field must have an integrity control that prohibits a null value. Any other required field may also have a null value control placed on it depending upon the policy of the organization. For example, a university may prohibit adding a course to its database unless that course has a title as well as value to the primary key, course-ID. Many fields legitimately may have null values so this control is to be used only when truly required.
- (vi) Referential Integrity: This control on a field is a form of range control in which the value of that field must exist as the value in some field in another row of same or different table. That is the range of legitimate values comes from the dynamic contents of a field in a data base table, not from some pre-specified set of values. Referential integrity guarantees that only some existing cross-referencing value is used, not that it is the correct one.

Question 5

- (a) Describe the benefits of SAN.
- (b) Explain the various views of a slide in MS-POWER POINT.
- (c) Explain the various tools available to protect the information from intrusion and misuse.
- (d) Define the following functions used in MS-EXCEL:
 - (i) NPV
 - (ii) LOG
 - (iii) LEN
 - (iv) ROUND
 - (v) COUNT

(5 + 5 + 5 + 5 = 20 Marks)

Answer

- (a) A Storage Area Network (SAN) is a dedicated, centrally managed, secure information infrastructure, which enables any-to-any interconnection of servers and storage systems. Following are the benefits of SAN:
 - (i) Removes data traffic: Like back up processes, from the production network giving IT managers a strategic way to improve system performance and application availability.
 - (ii) Improves data access: Using fiber Channel connections, SAN provides high speed network communication and distance needed by remote workstations and servers to easily access shared data storage pools.
 - (iii) Centralised Management of Data: IT managers can more easily centralize the management of their storage systems and consolidate backups, increasing overall system efficiency. The increased distances provided by Fiber Channel Technology

makes it easier to deploy remote disaster recovery sites. Fiber Channel and switched fabric technology eliminate single point of failure on the network.

- (iv) Unlimited network expansion: Unlimited expansion is possible with hubs and switches. Nodes can be removed or added with minimal disruption to the network.
- (b) PowerPoint offers five views:
 - (1) Normal View: This view gives small pane for text. It allows the user to frequently switch between text and objects on the slide.
 - (2) Outline View: This view gives largest pane for text, hence it is easy to work on a presentation. On the other hand, text is spread over several lines in normal view because the space for text is less.
 - (3) Slide View: This view makes it convenient to insert objects and modify them. This view shows how the text and objects appear on each slide. Using this view, user can work only on one slide at a time.
 - (4) Slide Sorter View: This view helps in moving the slides around but text/objects can not be rearranged on individual slides. This view shows all the slides at one time.
 - (5) Slide Show View: This view shows all the slides of the presentation one by one automatically if the time of each slide has been set up or slides can be viewed one by one on mouse click.
- (c) Various tools available to protect the information from intrusion and misuse are discussed below:
 - (1) Firewalls: These are the software which are installed on the web server to protect the server from hacking. Hackers are mischief makers who intentionally disable the site and whenever any user tries to open that site, its home page is not displayed. However, Firewall can also be implemented with the help of hardware like Nokia Checkpoint.
 - (2) Encryption: Before the transmission of data like transfer of credit card number on telephone line during E-Commerce transactions, data is encrypted so that no person can trap the data on the way. Encryption of data can be performed with the help of hardware as well as with the help of software.
 - (3) Message Authentication: Before providing access of data to the user, authentication of user can be done with the help of passwords. Organisation server may also be configured to accept the message only from the known persons.
 - (4) Site blocking: It is a software based approach which restricts the users to access certain sites. For example, in certain organisations, servers are configured in such a manner so that user cannot open the site. For example resume posting sites like Naukri.com, jobahead.com etc.
- (d) (i) NPV (values, rate): This function is used to calculate net present value of an

investment based on discount rate and a series of future payments.

- (ii) LOG(x): Returns the logarithm of a number to the base 10.
- (iii) LEN (text string): It returns the number of characters in the text string e.g. if text string = 'Examination', then this function will return 11.
- (iv) ROUND (x, n): To round off the number x to n number of decimal places e.g. if x = 2.1752 and n = 2 then = ROUND (x, n) will return 2.18.
- (v) Count (range): This function is used to count the number of items in the range of cells ignoring the blank cells.

Question 6

- (a) What is Image processing? Explain the steps required for image processing.
- (b) Discuss the objectives of Information Technology Act, 2000.
- (c) Explain the following techniques of audit used by internal auditors:
 - (i) System activity file interrogation.
 - (ii) Program comparison
- (d) Explain general management concerns in E-commerce. (5 + 5 + 5 + 5 = 20 Marks)

Answer

- (a) Image Processing: It is the process of entering an image, graph, design, drawing or photograph into the computer with the help of digitizing. Digitizing is a process of converting the graphical information into digital form. Image processing also known as Document Imaging is a step towards paperless office. There are five steps required for document imaging.
 - (1) Data Capture: Paper documents are entered into the computer with the help of image scanner. Image scanner converts the graphical information into digital form. Printers are available in the market having removable printing head which can be replaced with scanning head, enabling the printer to work as image scanner. There are two types of scanners:
 - (a) Page Scanner (Flat bed scanner): This scanner is used to scan the large images by placing the document on a flat surface and giving the command with the help of scanner software using computer.
 - (b) Hand held scanner: This scanner is used to scan small images by holding the scanner in hand and moving the scanner on the document.
 - (2) Indexing: For fast retrieval of the stored documents, scanned images are indexed on the basis of some criteria like Vendor Code or purchase order number.
 - (3) Storage: Scanned document files are stored on auxiliary storage media for future reference. Since size of the scanned files is more, therefore, compact disk (CD's) or DVD's are used as storage media.

- (4) Retrieval: Document management software allows the user to access any required information from the stored files on the basis of various parameters like Indexed key, key word etc. The software can automatically mark the optical disks (CD's) so that when any information is required to be accessed, then software may tell the number of that CD storing the desired information.
- (5) Output: Hard copy of the scanned documents can be printed with the help of printers and even can be sent to another person through E-mail.
- (b) Objectives of the Information Technology Act, 2000
 - (a) To grant legal recognition to transactions carried out by means of EDI and E-Commerce in place of paper based methods of communication.
 - (b) To give legal recognition to digital signatures for authentication of any information.
 - (c) To facilitate electronic filing of documents with Government Departments.
 - (d) To facilitate electronic storage of data.
 - (e) To facilitate and give the legal recognition to electronic fund transfers between bank and financial institutions.
 - (f) To give legal recognition for keeping books of accounts in electronic form by bankers.
 - (g) To amend the Indian Penal Code, the Indian Evidence Act, the Banker's Book Evidence Act and Reserve Bank of India Act.
- (c) i) System Activity File Interrogation: Many computer operating systems automatically create a log file listing all the exceptional events occurring in the system. This log file is stored on hard disk and review of this file helps in identification of exceptional events as listed below:
 - The use of utility program instead of application program to change the data file.
 - Attempt to break password to gain access of the system.
 - The running of an application program without normal sequence.
 - Change in application programs.
- (ii) Program Comparison: This tool compares two different versions of the same program to check that they are identical. Software is available to do this comparison on source code as well as on object code. This tool can be used in the following situations:
 - Comparing the program actually implemented with the one tested and accepted by user.
 - Comparing the programs installed at different locations.
 - Comparing the presently installed version with a copy of previously tested version under the control of the auditor.

Any difference between the two copies will require programming skill to know the impact of changes on the output.

(d) General Management Concerns in E-Commerce are as follows:

- (1) Loss of Paper audit trail: Since no paper work is involved in doing the business transactions electronically, hence keeping the track of business activities will be difficult.
- (2) Business Continuity: In E-Commerce, all the transactions are done with the help of computers, hence if computer system fails then entire business organization will be paralyzed.
- (3) Exposure of data to third parties: Due to sharing of data among organisations, there is possibility of exposure of secret information to other parties.
- (4) Record retention: Electronic information is required to be kept safely as a statutory requirement, therefore organisations will have to take appropriate measures for the safety of data.
- (5) Segregation of duties: There are more chances of fraud in an electronic environment. Hence, duties of various persons working in electronic environment must be properly defined, in order to fix their responsibilities at later stages.
- (6) Legal Liability: The inability to complete transactions or meet deadlines, or the risk of inadvertently exposing information of trading partners poses legal risks.

(Note: Students are required to give any 5 points)

Question 7

Write short notes on the following. Answer any four:

- (i) Voice messaging
- (ii) Wireless networks
- (iii) File management system
- (iv) Diagnostic routines
- (v) White box approach for audit.

(5 × 4 = 20 Marks)

Answer

- (i) Voice Messaging: This communication approach is similar to Electronic mail except in this approach, audio messages rather than text messages are processed. A sender speaks on the phone giving the name of the recipient and message. Sender's voice signals are converted to digital signals and stored. The system then transfers the message to the recipient. The message is converted back to analog form when it is received by the recipient. Recipient hears the same voice as it had been spoken by the sender. Voice messaging requires a computer with the ability to store the message by converting it into digital form and converting back to analog form upon retrieval. Main

advantage of voice messaging over electronic mail is that the sender need not have to type the message.

- (ii) **Wireless Networks:** People on the road often want to use their portable computers like Laptop or Notebook computers to send and receive electronic mails, read remote files from the server of their office and to surf the Internet from anywhere on land, sea or air. Since a wired network is impossible in cars and aeroplanes, hence it resulted in the development of wireless network. WAP (Wireless Application Protocol) is the protocol used in Wireless communication. Laptop computers with wireless card are available in the market. Wireless technology known as Bluetooth allows the user to transfer the data between computer and Mobile Phone/Digital Camera. Airports and some Indian Universities have been converted to Wireless fidelity (Wi-Fi) zones which are allowing users to use Internet services anywhere within the premises of Airport.

Wireless networks are of great use for those persons who remain away from their home/office for most of the time. Another use of wireless network is for the rescue workers at the disaster sites like fires, floods or earthquake sites where telephone system gets destroyed.

- (iii) **File Management System:** In this system, different users work on their independent computers and maintain their own data files. Each user has its own application software according to the requirements which was either developed in-house or got developed from external software agency according to the requirements. Instead of getting integrated software developed, different users have independent modules for data processing. Such system of maintaining files creates many problems as discussed below:
 - (a) **Data redundancy:** When same data files are stored at different locations, then it is called data redundancy. It causes problem when the data has to be updated. Different users may use same data as to occur inconsistency among different files.
 - (b) **Lack of Data integration:** Data files of different users are not integrated with each other, therefore changes made by one user are not made in each file automatically. It is an expensive and time consuming process for an organisation.
 - (c) **Data inconsistency:** Lack of Data integration create data inconsistency. When at a particular time, data stored in different files does not reconcile with each other, then it is called data inconsistency.
 - (d) **Program-data dependence:** Software modules being used by different users are developed in high level programming languages like BASIC, COBOL etc. These high level languages use different file formats. Therefore, when program written in one programming language is required to be changed in another language, then it becomes essential to change the format of data files also.
- (iv) **Diagnostic Routines:** It is a system software which is usually a part of operating system and is provided by the computer manufacturer. These are those programs which help the user in debugging of program as well as to find out the details of various equipments used in the computer, like:

1. What type of Processor is installed in the computer like P-III or P-IV and its speed?
 2. What is total amount of main memory like 128MB/256MB?
 3. What type of keyboard is attached with the computer like 101 Keys/104 keys/Multimedia Keyboard?
 4. What is display type like VGA/SVGA?
 5. What type of mouse is attached with computer like 2 buttons/3buttons/scroll mouse/Mechanical Mouse/Optical Mouse?
 6. Is separate math coprocessor present in computer?
 7. Where is BIOS (Basic I/O) manufacture like AWARD BIOS or ANI BIOS?
- (v) White Box Approach for Audit: Presently, computer system has progressed to a point where entire processing cycle occurs within the computer system. Therefore, traditional audit trial has disappeared. Hence, it becomes necessary to examine the internal working of the computer system. The auditor can verify the progress himself and get technically satisfied that the system, internal checks, controls, error detection and data security procedures are satisfactory. Auditor can use test checks to keep the system in operation. By acquiring the necessary skills, the auditor can use the computer itself as an audit tool to improve the quality of his own audit and can reduce time spent on detailed verification of transactions.

In this type of white box approach, the auditor's primary concern includes the system of controls, examination and testing of computer implemented controls.

SUMMARY OF EXAMINERS' COMMENTS ON THE PERFORMANCE OF CANDIDATES

PAPER – 4 : COST ACCOUNTING AND FINANCIAL MANAGEMENT

General Comments

Overall performance of the candidates was average. Candidates are required to practice as many practical questions as possible under examination conditions by referring to the Study material, Revision Test Papers, Suggested Answers and Reference books. Performance revealed lack of in-depth knowledge and rigorous study. The candidates need to understand each and every topic of the subject conceptually and also fine tune their writing skills including presentation of data.

Specific Comments

Question 1.(a) This was a practical question part requiring a sound understanding of Process Costing. Most of the examinees were unable to compute the equivalent production units and statement of cost correctly. Subsequently, Process account, Normal loss accounts and Abnormal loss accounts were not made correctly by the students.

(b) This theoretical part required basic knowledge of Activity Based Costing. Many of the examinees explained Unit costing in place of Unit level activities and Batch costing in place of Batch level activities.

Question 2. (a) This question requires basic understanding of Integrated accounting system. In this theory question part some of the examinees wrote about the advantages of double accounting system instead of Integrated Accounting. However most of the candidates have attempted the answer well.

(b) This numerical part requires fundamental understanding of Operating Costing. Very few students answered all the three parts correctly. The words 'per month' and 'per year' given in the question were ignored by majority of the students. They were confused regarding number of club members and number of library members resulting in wrong calculation of subsidy.

Question 3.(a) In this question examinees were required to compute the ratio of the new material mix at the same quantum of profit as at the existing level. This numerical part was attempted by a handful number of candidates and many out of them could not calculate the material mix properly.

(b) In this theoretical part conceptual understanding of different types of cost, audit and preliminary understanding of inventory management was required. Many students have given vague and sketchy answers for 'discretionary costs' and 'proprietary audit'. In other parts of this question examples were not cited by the candidates.

Question 4.(a) This was a practical question part requiring basic understanding of Operating Costing. Majority of the candidates failed to find out the total cost and subsequently cost of each type of room. Many students were not able to formulate the equation to find out the cost of one suite correctly.

(b) In this theoretical part related to labour, majority of the students have written formula of

Rowan premium bonus system instead of explaining what has been asked for in the question.

Question 5.(a) In this numerical question part examinees are required to have a basic knowledge of concepts of reconciliation between cost accounting records and financial accounting records. Many of the candidates could not calculate the costing profit correctly. However, reconciliation part was attempted well by most of the examinees.

(b) This theoretical question part requires a sound understanding of Contract Costing and Inventory Management. Examiners have reported a lack of understanding of concepts related to Contract Costing. Retention money in Contract Costing has not been explained correctly by majority of the candidates. A few candidates were confused between 'Economic batch quantity' and 'Economic Order Quantity' and have answered on wrong lines.

Question 6.(a) Being a compulsory question, it was attempted by a number of candidates. Majority of the candidates computed the Balance Sheet items on correct lines. However only a few candidates correctly computed the items of Profit and Loss A/c and presented them in a proper manner.

(b) This theoretical question was also not attempted properly by most of the candidates.

Question 7.(a) A large percentage of the candidates attempted this question. However, only a very few candidates computed cost of funds for additional amount of debtors correctly. Therefore majority of the candidates arrived at the wrong conclusion.

(b) This part of the question was well attempted by a majority of candidates however few candidates properly covered all the services provided by the factoring agencies in their answers.

Question 8.(a) This practical question part required candidates to compute the WACC. A conceptual understanding of cost of capital was needed to solve the problem on correct lines. However, most of the candidates could not work out correctly the cost of equity and cost of preference share capital.

(b) A large number of candidates did not attempt this part of the question satisfactorily. Majority of the candidates confused 'Propositions made by Modigliani and Miller' as 'Assumptions made by Modigliani and Miller' and hence answered the question on wrong lines.

Question 9.(a) Majority of the candidates attempted this question and majority of candidates calculated cash flows upto 4 years correctly but faltered in the calculation of depreciation (including the loss on disposal of asset) in the 5th year (terminal year). Therefore majority of the candidates incorrectly computed the NPVs at the given rates and IRR was computed wrongly.

(b) This theory part required understanding of Global Financial Market. Most of the candidates were not able to attempt the question on correct lines and majority of the candidates gave vague answers.

PAPER – 5 : INCOME-TAX AND CENTRAL SALES TAX

General comments

Overall performance of the candidates was not very satisfactory, particularly in problem oriented questions. Most of the candidates have not properly presented the solution to computational problems stepwise in an orderly manner. In the case of True/False questions, many candidates have simply answered True or False, without giving proper reason for their answer by mentioning relevant provisions of the Act. Candidates have exhibited poor knowledge of the basic provisions of the Act and also of the recent amendments to the Income Tax Act. Other deficiencies are very poor handwriting, lack of expression and spelling and grammatical mistakes.

Specific Comments

Question 1.(a) Most of the candidates have not understood the problem and failed to compute income-tax correctly. Some common mistakes were:

- (i) Most of the candidates have not considered stamp valuation as sale consideration for calculating capital gain.
- (ii) Income from salary from a City Care Centre was included under the head 'Income from other sources'.
- (iii) Winnings from Lotteries have not been grossed up and lottery expenses have been wrongly deducted.
- (iv) Candidates have not considered agricultural income for rate purposes.
- (v) Majority of the candidates have taken the maturity value of LIC as income from other sources, though it is exempt from tax.
- (vi) Some of the candidates have shown honorarium of Rs. 14,000/- for valuing medical examination answer books, under the head 'Profits and gains from business and profession' instead of showing the same under the head 'Income from other sources'.
- (b) Most of the candidates were not aware of the provisions regarding apportionment of depreciation when there is conversion of proprietary business into a company. Block of assets concept was not clear to many candidates.

Question 2. (First Alternative)

- (a) Many candidates have not understood the concept of Marginal Relief. Hence, calculations with regard to the same were also not correct.
- (b) Most of the candidates were not aware of the provisions of the section 80QQB and have got confused with deduction for political parties. Their answers were very general without explaining the relevant provisions of the Act.

Question 2. (Second Alternative)

(a) Many candidates were not aware of the provisions contained in section 80IB. They have not mentioned the specific provisions contained in section 80-IB(7A) and (7B) relating to multiplex theatres and convention centres.

(b) Most of the candidates have not answered correctly since they have not understood the provisions contained in section 45(2). Some of the candidates have wrongly treated the entire income on conversion of capital assets into stock in trade as business income.

Question 3.(a) (i) Most of the candidates were not aware of the amendment made in section 2(24) by the Finance Act, 2006 and have written that voluntary contribution received by charitable trusts are exempt. Some have explained the distinction between charitable trust, university and educational institutions. Some others have written false without any reasons.

(iii) Most of the candidates were not aware of the provisions of section 148 regarding the time limit to issue notice in case of an amount exceeding Rs.1 lakh. Except a few candidates, none of them could mention that the time limit was 6 years.

(v) Some of the candidates have given lengthy reasoning, without stating true or false.

(b) (iii) Most of the candidates have answered Rs.195,000 instead of Rs.185,000 as exemption limit of income available to a senior citizen for A.Y. 2007-08.

(iv) Most of the candidates have not correctly answered the time limit for filing an appeal.

(v) Some of the candidates have considered the amount of Rs. 65,000/- as deductible under section 80C.

Question 4.(a) Most of the candidates were not able to answer correctly since they were not aware of the provisions of section 43B. Many candidates wrote the wrong answer by giving the provisions of section 40A(3) on disallowance of cash expenditure exceeding Rs. 20,000/- instead of section 43B on deduction to be allowed on actual payment basis.

(b) This question pertains to the Scheme of submission of return through Tax Return Preparer (TRP), which was introduced by the Finance Act, 2006. Most of the candidates have misunderstood TRP as Electronic filing system. Some of the candidates have wrongly explained provisions of Section 139(1A) and 139(1B).

(c) Most of the candidates misunderstood section 80GG with section 80G on deduction on account of donation.

(d) Most of the candidates have not explained the provisions of section 10AA clearly. They have written vague answers and other benefits derived by the units in SEZ on account of sales tax and other taxes.

Question 5. (a)(ii) Most of the candidates have stated 'False', but reasons were not correct.

(v) This pertains to VPP sale. Candidates have not correctly understood the statement and have answered on the basis of normal inter state sale movement from one State to another.

Question 5. (b)(v) Some candidates have wrongly written that the authority to declare goods of special importance lies with the Central Sales Tax Authority.

Question 6. (a) Most of the candidates have not answered this part with reference to provisions contained in Central Sales Tax Act and have discussed penalties in general.

(b) This question pertains to consideration for selection of goods of special importance. Most of the candidates have got confused and explained section 14 in detail, without mentioning the points to be considered for selection of goods of special importance. Some of the candidates have misunderstood consideration as something in return (i.e. sale price)

(c) Most of the candidates do not have proper knowledge of the provisions relating to forfeiture of security. Some of the candidates explained provisions regarding procedure of registration and taking of security instead of on forfeiture of security.

PAPER – 6 : INFORMATION TECHNOLOGY

General Comments

Adequate subject knowledge and competency is required to attempt the question correctly that was not reflected in answer sheet prepared by the student. Student wrote answer without understanding the requirement of the question. Student need to understand the basic concepts of the usages of Information Technology in the particular domain. They have to improve the subject knowledge as well as language skill for better performance.

Specific Comments

Question 1.(a) Most of the student attempted this question and performed well.

(b) Some of the students fails to explain the meaning of 'Gateways', 'Duplex Printing' and 'Asymmetric Crypto System' correctly. The understanding of the technical things are required for the student to give appropriate answers.

(c) Very few students did not explain the meaning of 'Use of Firewall' and 'Use of Routers'. Although the performance is satisfactory.

(d) Very good performance by majority of the students.

Question 2. (i) Answered given by most of the students with an average performance. Lack of giving technical words at the right places is major problem of the students.

(ii) Average number of students do not know the technical differences between 'Logical Record and physical record'.

(iii) The answers are readily available in the course material and hence, generally, well answered by almost all the students.

(iv) Answered by majority of the students and performed well.

(v) More than average number of students attempted this question nicely.

Question 3.(a) Most of the students attempted this question and performed well.

(b) More than average number of students attempted this question and performed well.

(c) Average number of students attempted this question and the performance is not satisfactory. Students are required to understand the importance and utility of 'Flow Charts' in programming. They must understand the basic symbol used in Flow chart.

Question 4.(a) Answered by most of the students with average performance.

(b) Attempted by the majority of the student and performed satisfactory.

(c) Performance is not satisfactory. Most of the students lacked in understanding of the question. Description is given more on DBMS rather than Data Integrity Control.

Question 5.(a) Mostly all the students has given corrected answers and secured goods marks.

(b) Answered by most of the students with good performance.

(c) Many of the students attempted this question nicely.

(d) Some of the students were not able to explain most of the MS-Excel function with syntax command.

Question 6.(a) Most of the students attempted the question nicely and performed well.

(b) Most of the students answered as it is given in study material.

(c) Students lacked understanding the questions and answered wrongly. They must go through with the procedure and techniques used in computer based auditing.

(d) Performance is not satisfactory. Only few students answered 'Management concern of e-commerce' and rest answered the 'Benefit of e-commerce' i.e. wrong.

Question 7.(i) Mostly all the students attempted this question correctly and performed well.

(ii) Satisfactory performance by majority of the students.

(iii) Most of the students attempted the question but answer was not satisfactory. Only few stated about the Data Integrity and Inconsistency'.

(iv) Many of the students have answered wrongly without understanding the basic concept of operating system.

(v) Attempted by the majority of the students and performed well.



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