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Answer Paper	
Direct Tax Laws	**Duration**: 80
Details: Test – 2	**Marks**: 40

Instructions:

- All the questions are compulsory
- Properly mention test number and page number on your answer sheet, Try to upload sheets in arranged manner.
- In case of multiple choice questions, mention option number only Working notes are compulsory wherever required in support of your solution
- Do not copy any solution from any material. Attempt as much as you know to fairly judge your performance.

ANS 1:

Section 23 of the Income-tax Act provides relief to the taxpayer by allowing him an option to claim nil annual value in respect of any two houses, declared as self-occupied, instead of one such house as provided earlier. Besides this section 24 of the Income-tax Act has been amended to provide that the monetary limit of deduction on account of interest payable on borrowed capital i.e. Rs.30,000/ Rs.2,00,000 shall continue to apply to the aggregate of the amounts of deduction in case of more than one self-occupied houses.

Thus assessee has the following options:

Option I: House I and II self occupied and House III – deemed to be let out.

Option II: House I and III self occupied and House II – deemed to be let out.

Option III: House II and III self occupied and House I - deemed to be let out.

The lowest value of house property amongst the above options shall be offered for taxation.

Hence, the Income from house property shall be computed as under:

(1) Computation of income from houses when they are deemed to be let out (amount in Rs.)–

Particulars	**House –I**	**House - II**	**House - II**
Gross Annual Value **[Note-A]**	1,00,000	1,65,000	12,40,000
Less: Municipal taxes paid **[Note-B]**	Nil	9,200	20,000
Net Annual Value	**1,00,000**	**1,55,800**	**2,20,000**
Less: Deductions under section 24 –			
(a) Statutory Deduction @ 30% of NAV	30,000	46,740	66,000

(b) Interest on loans	1,80,000	80,000	75,000
Income from house	**-1,10,000**	**29,060**	**79,000**

Notes:

(A) GAV = Municipal Value or Fair Rent, whichever is higher subject to maximum of Standard Rent.

(B) Municipal taxes actually paid shall only be allowed as deduction.

Computation of income from houses when they are treated as self-occupied (amount in Rs.) –

Particulars	House –I& II	House - I & III	House - II & III
Annual Value [Since both the houses are self occupied]	Nil	Nil	Nil
Less: Interest on loans [House - I:Rs.1,80,000 and House - II : Rs.80,000 (Restricted to 2,00,000)	2,00,000	2,00,000	1,55,000
Income from house property	**-2,00,000**	**-2,00,000**	**-1,55,000**

(2) Hence the taxable value shall be arrived as under (amount in Rs.):

Option	Total
Option I: House I and II self occupied and House III- deemed to be let out	-1,21,000

Option II: House I and III self occupied and House II-Deemed to be let out	-1,70,940
Option III: House II and III self occupied and House I- deemed to be let out	-2,65,000

Since the lowest value is in option III, hence the Income from house property will be Rs. (-2,65,000).

(6 Marks)

ANS 2:-

Computation of Income of Babu under the Head "Salaries" (amounts in Rs.)

Basic Salary (Rs. 25,000 x 10)	2,50,000
Dearness allowance (Rs. 10,000 x 10) [WN-1]	1,00,000
Bonus (Rs. 50,000 x 10)	5,00,000
Value of Accommodation [WN-2]	1,52,500
Sweeper salary paid by employer (Rs. 1,500 x 10)	15,000
Watchman salary paid by employer (Rs. 1,500 x 10)	15,000
Car facility [WN-3]	27,000
Club facility [WN-4]	Nil
Education facility to children [WN-5]	Nil
Interest free housing loan (Rs. 5,00,000 x 12.25% x 6/12)	30.625
Interest free computer loan (Rs. 50,000 x 15.25% p.a. x 3/12)	1,906

Gross salary	**10,92,031**
Less: Standard deduction u/s 16(ia)	50,000
Income under the head salaries	**10,42,031**

Working Notes:

1) It is assumed that DA forms the part of salary for retirement benefits.

2) It is assumed that the place of accommodation has population exceeding 25 lakhs and accordingly, the taxable value of Rent free furnished accommodation shall be computed as follows **(amounts in Rs)-**

Valuation of rent free accommodation	15% of salary
Value of rent free accommodation (Rs. 8, 50,000 x 15%)	1,27,500
Add: Furniture (10% p.a. of original cost of furniture) [Rs. 3,00,000 x 10% x 10/12]	25,000
Taxable value of furnished accommodation	**1,52,500**
Salary for rent free accommodation:	
- Basic pay	2,50,000
- DA	1,00,000
- Bonus	5,00,000
	8,50,000

3) The car is used partly for personal and partly for official use. Assuming that the maintenance and running expenses are met by the owner-company, value of car facility = (Rs. 1,800 + Rs. 900) x 10 = Rs. 27,000

4) The initial fee for corporate membership is exempt from tax

5) It is assumed that the cost of education per child does not exceed Rs. 1,000 p.m.

ANS-3:

Computation of capital gains on slump sale of Unit 1 (amount in Rs):

Full value of consideration **[Fair market value on 1-4-2021]**	14,82,500
Less: Expenses on sale	38,000
Net sale consideration	**14,44,500**
Less: Net worth **[WN-1]**	11,73,125
Long-term capital gain	**2,71,375**

Working Notes:

(1) Computation of Full value of consideration (amount in Rs.):

Fair market value of the capital assets transferred by way of slump sale	
Building, being an immovable property [stamp duty value on 1-4-2021, being the date of slump sale] [A]	10,00,000

Machinery [Book value as appearing in the books of accounts] [B]			4,00,000
Debtors (Book value as appearing in the books of accounts] [C]			2,00,000
Patents [Book value as appearing in the books of accounts] [D]			2,50,000
			18,50,000
Less: Liabilities of Unit 1[Rs. 29,50,000 - Rs.1,20,000 – Rs.2,62,500] [L]		25,67,500	
Excluding:			
(i) Own Capital	17,00,000		
(II)Revaluations reserve	5,00,000	22,00,000	3,67,500
Fair market value of the capital assets transferred by way of slump sale [A+B+C+D-L] [FMV1]			**14,82,500**
Fair market value of the consideration received or accruing as a result of transfer by way of slump sale value of the monetary consideration received] **[FMV2]**			14,00,000
Full value of consideration (Higher of FMV1 or FMV2]			**14,82,500**

(2) Computation of net worth of Unit 1 of Simran Enterprises:

Building (excluding Rs.5 lakh on account of revaluation)		8,00,000
Machinery		4,00,000

Debtors		2,00,000
Patents (see note 3 below)		1,40,625
Total assets		**15,40,625**
Less: Creditors[Rs.3,50,000×25%]	87,500	
Bank Loan [Rs.4,00,000×70%]	2,80,000	3,67,500
Net worth		**11,73,125**

(3) Written down value of patents as on 1-4-2021:

Value of patents	Rs.
Cost as on 1-7-2019	2,50,000
Less: depreciation @25% for Financial year 2019-20	62,500
WDV as on 1-4-2020	**1,87,500**
Less: Depreciation for Financial Year 2020-21	46,875
WDV as on 1-4-2021	**1,40,625**

For the purposes of computation of net worth, the written down value determined as per section 43(6) has to be considered in the case of depreciable assets. The problem has been solved assuming that the Balance Sheet values of Rs. 4 lakh and Rs.8 lakh (Rs.13 lakh-Rs.5 lakh) represent the written down value of machinery and building, respectively, of unit 1.

(8 Marks)

ANS-4

The answer to the case study is discussed as under-

(i) Issue Involved: Can consideration for supply of software embedded in hardware tantamount to 'royalty' under section 9(1)(vi)?

(ii) Provisions applicable: As per section 9(1)(vi), income by way of royalty payable by a person who is a non-resident would be deemed to accrue or arise in India, where the royalty is payable in respect of any right, property or information used or services utilized for the purposes of a business or profession carried on by such person in India or for the purposes of making or earning any income from any source in India.

For this purpose, royalty includes transfer of all or any right for use or right to use a computer software irrespective of the medium through which such right is transferred.

(iii) Analysis: The High Court in CIT v. Alcatel Lucent Canada [2015] 372 ITR 476 (Del) observed that-

(a) The software that was loaded on the hardware did not have any independent existence;
(b) The software supply is an integral part of GSM mobile telephone system and is used by the cellular operators for providing cellular services to its customers;
(c) The software is embedded in the system and there could not be any independent use of such software;
(d) This software merely facilitates the functioning of the equipment and is an integral part of the hardware.

Where payment is made for hardware in which the software is embedded and the software does not have independent functional existence, no amount could be attributed as 'royalty' for software in terms of Section 9(1)(vi).

(iv) Conclusion: Therefore, the action of the Assessing Officer in treating the consideration for supply of software embedded in hardware as royalty under section 9(1)(vi) is not correct.

(6 Marks)

ANS 5:-

The issue under consideration in this case is whether the order of assessment of deceased person completed without bringing the legal representative on record is bad in law. As per section 159(2), for making a reassessment of the income of the deceased person, any proceeding taken against the deceased before his death shall be deemed to have been taken against the legal representative and may be continued against the legal representative from that stage.

In a case where an assessee dies pending any assessment proceedings, the Assessing officer is required to pass appropriate orders of assessment after due notice to legal representative of deceased assessee. However, in the instant case, the Assessing officer continued the assessment proceedings without bringing Mr. Nitin, the legal heir, on record by issuing any notice for such proceedings after the death of his father on 15-01-2021. Therefore, the contention of the Mr. Nitin that the order of assessment is bad in law is correct.

Note: The facts of the case are similar to the facts in CIT v. Dalumal Shymamal [2005] 276 ITR 62 wherein the above issue came up before the MP High Court. The above answer is based on the rationale of the High Court in the said case.

(6 Marks)

MCQ's

1. D

2. B

The value of perquisite shall be computed as follows –

(i) In this question shares of M/s. MNO Ltd. are traded on more than one stock exchange (both, BSE and NSE) on the date of exercise of the option i.e. on 15-3-2021, hence, as per Valuation Rules, the average of the opening and closing prices on the recognised stock exchange, which records highest trading volume shall be taken to be the fair market value of each option.

(ii) Since NSE recorded the higher trading volume, hence, FMV on that date on NSE = 36,000 shall be taken to be the FMV for the purpose of valuation of perquisite.

(iii) Value of perquisite = (FMV - Exercise Price) * No. of shares = Rs (600 - 250) * 500 shares = 1,75,000.

(iv) The taxability of perquisite will arise in the year in which shares are allotted or transferred to employee i.e. in the previous year 2021-22. Even if the option is granted for providing know-how, the same will fall within the meaning of 'sweat equity shares' and, therefore, section 17(2)(vi) shall apply in the same manner as given above.

3. D

Explanation: As per Rule 4, the amount of rent which the owner cannot realise (Unrealised Amount) shall be equal to the amount of rent payable but not paid by a tenant of the assessee and so proved to be lost and irrecoverable, where –

(i) The tenancy is bona fide;

(ii) The defaulting tenant has vacated, or steps have been taken to compel him to vacate the property:

(iii) The defaulting tenant is not in occupation of any other property of the assessee; and

(iv) The assessee has taken all reasonable steps to institute legal proceedings for the recovery of the unpaid rent or satisfies the Assessing Officer that legal proceedings would be useless.

4. A

Explanation: In the case of a capital asset, being the right to subscribe to any financial asset which is renounced in favour of any other person the period of holding of the capital asset shall be reckoned from the date of the offer of such right by the company or institution, as the case may be, making such offer.

5. C

Explanation: Computation of Capital Gains-

Particulars	**Rs.**
Full Value of consideration	20,00,000
Less: Indexed cost of acquisition (Rs. 5,50,000 ×317 ÷100)	17,43,500
Long term gains	**2,56,500**