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Black Money and Tax Evasion in India

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ABSTRACT

Of late, the issue of corruption and black money has come in the forefront after a series of financial scandals. Generation of black money and its stashing abroad in tax havens and offshore financial centers have dominated discussions and debate in public fora during the recent past. Members of Parliament, the Supreme Court of India and the public at large have unequivocally expressed concern on the issue, particularly after some reports suggested estimates of such unaccounted wealth being held abroad. After uproar in Parliament, Government of India came out with a White Paper on Black Money in May 2012. The White Paper presented the different facets of black money and its complex relationship with policy and administrative regime in the country. It also reflected upon the policy options and strategies that the Government had been pursuing in the context of recent initiatives, or need to take up in the near future, to address the issue of black money and corruption in public life. The objective of this paper is to explain various facets and dimensions of black money and tax evasion and their complex relationship with the policy and administrative regime in India. It describes the factors which lead to the generation of black money, and records various estimates of black money and tax evasion. It also presents the measures/strategies that the Government of India has been pursuing to tackle this issue, especially recent initiatives and developments.

***Keywords**: Black money, tax evasion, tax havens*.

1.0 Black Money Defined

There is no uniform and universally acceptable definition of black money in fiscal literature. Generally speaking, the term *black money* stands for money earned by illegal means and kept secret and unaccounted for.

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It is widely used for smuggling activities, hoarding of scarce commodities (for the purpose of speculation, profiteering, and black marketing), bribing government officials, financing political activities, and ostentatious living.Secret business deals through black money in turn lead to tax evasion and a vicious circle is created in which one evil thrives on the other.

The term *black money* has many synonyms including *underground economy*, *parallel economy*, *shadow economy unofficial economy, and unaccounted economy*. All these terms usually refer to any income on which the taxes imposed by government or public authorities have not been paid. Thus, *black money* can be defined as assets or resources that have neither been reported to the public authorities at the time of their generation nor disclosed at any point of time during their possession.

In addition to wealth earned through illegal means, the term black money would also include legal income that is concealed from public authorities: (a) to evade payment of taxes (income tax, excise duty, sales tax, stamp duty etc), (b) to evade payment of other statutory contributions, (c) to evade compliance with the provisions of industrial laws, and/or to evade compliance with other laws and administrative procedures.

Black money may be generated in two ways. Firstly, money may be generated through illegitimate activities not permissible under the law—like drug trade, terrorism, and corruption—and which are punishable under the legal framework of the state. Secondly, money may be generated and accumulated by failing to pay the dues to the public exchequer in one form or the other. In this case, the activities undertaken by the perpetrator could be legitimate and otherwise permissible under the law of the land but he fails to report the income so generated, comply with the tax requirements, or pay the dues to the public exchequer, leading to the generation of unaccounted wealth.

The comparison of the above two ways in which black money is generated is important to understand the problems and adopt appropriate policy measures to curb and control black money. It is clear that the first category is one where an iron fist is required on the part of government and its various law enforcing agencies. However, it is the second category where the issue becomes far more complex and may require new legislations/modification of existing laws and reforms in current policies and strategies to promote compliance with laws (particularly tax laws), regulations, and rules. The revamped institutional structure should also discourage the active economic agents of society from generating, hoarding, and illicitly transferring abroad such unaccounted wealth.

2.0 Sectors/Activities more Prone to Generation of Black Money and Tax Evasion

The source of generation of black money can lie in any sphere of economic activity. Nevertheless, there are certain sectors and activities which are more prone to black money generation. These include, *inter alia*, the following:

1. Land and real estate transactions.
2. Bullion and jewellery dealings.
3. Complex financial market transactions (derivatives).
4. Charitable (non-profit) activities.
5. Informal sector and cash economy.
6. Self-employed professionals.
7. External trade and transfer pricing.

Land and Real Estate Transactions: Due to rising prices of real estate, the high tax incidence applicable on real estate transactions in the form of stamp duty and capital gains tax can create incentives for tax evasion through under-reporting of transaction price. This can lead to both generation and investment of black money. The buyer has the option of investing his black money by paying cash in addition to the documented sale consideration. This also leads to generation of black money in the hands of the recipient. [1]

Bullion and Jewellery Dealings: Cash sales in the gold and jewellery trade are quite common and serve two purposes. The purchase allows the buyer the option of converting black money into gold and bullion, while it gives the trader the option of keeping his unaccounted wealth in the form of stock, not disclosed in the books or valued at less than market price.

Complex Financial Market Transactions: Financial market transactions can involve black money in different forms. Rigging of markets by the market operators is one such means. This may involve use of dummy companies, trading in derivatives [2], participatory notes (PNs) [3] and other forms of manipulated trading.

Charitable (Non-profit) Activities: Taxation laws allow certain privileges and incentives for promoting charitable (non-profit) activities. Misuse of such benefits and manipulations through entities claimed to be constituted for non-profit motive are among possible sources of generation of black money.

Generally, charitable trusts are not required to pay tax on donations received by them. Similarly, income tax laws allow charitable contributions as deductions from taxable income. Since marginal rates of tax are high at upper brackets of income, charitable contributions are less costly to wealthy people.

These provisions are sometimes misused in the sense that donors exercise considerable control in managing the affairs of trusts/institutions to which charitable contributions are made. Private or family interest in the management of charitable trusts leads to control in the use of what are essentially public funds. Family control over a charitable trust generally leads to promoting private interest, defeating in the process the essential purpose of the tax concession. To quote, "Charitable organisations, non-government organisations (NGOs), and associations receiving foreign contributions are required to file an annual return to the Ministry of Home Affairs in Form FC-3. In the said form, only the name and address of the foreign donors are mentioned, with no further details of the beneficial owners. It is possible that in many such cases, the black money generated by Indians is being routed back to India." (Government of India, Ministry of Finance, 2012, para 2.8.5)

Informal Sector and Cash Economy: In its Report on Definitional and Statistical Issues Relating to the Informal Economy, submitted in 2008, the National Commission for Enterprises in the Unorganized Sector (Chairman: Arjun Sengupta), defined unorganized (informal) sector as the "sector consisting of all unincorporated private enterprises owned by individuals or households engaged in the sale and production of goods and services operated on a proprietary or partnership basis and with less than ten total workers". [4]

The issue of black money is related to the magnitude of cash transactions in the informal economy. Factors like dependence on agriculture, existence of a large informal sector, and insufficient banking infrastructure with large un-banked and under-banked areas contribute to the large cash economy in India.

Self-employed Professionals: Although evasion of tax is a common tendency among people belonging to different groups, opportunities for it vary according to the nature of income earned by taxpayers. In the case of income from salaries and interest from deposits, evasion is less likely because of proper recording and auditing of transactions, and deduction of tax at source. However, opportunities for tax evasion are very large in the case of self-employed in business and professions. Doctors, lawyers, architects, property dealers, individual contractors, jewellers, caterers, event managers can evade taxes more easily than others. They can insist on their customers to pay them in cash or accept invoices which underestimate the payment.

Moreover, salaried persons envy tax evasion opportunities available to self-employed professionals and retail traders, and are tempted to conceal their incomes from non-salary sources.

External Trade and Transfer Pricing: Differing tax rates in different countries can create perverse incentives for corporations to shift taxable income from jurisdictions with relatively high tax rates to jurisdictions with relatively low tax rates as a means of minimising their tax liability. For example, a foreign parent company could use internal *transfer prices* for reducing its worldwide tax payment. In fact, transfer pricing [5] has emerged as the biggest tool for generation and transfer of black money.

3.0 Tax Evasion Defined

Tax evasion exists in all countries, though in varying degrees. It is a serious problem in developing countries which are in the process of evolving their tax systems. Tax evasion is an illegal attempt to reduce the tax payable by deliberately under-reporting or not reporting taxable incomes or concealing one's true *state of affairs* from tax authorities. Tax evasion is a criminal offence and if detected is punishable by financial penalties or even by imprisonment or both.

3.1 Tax evasion and tax avoidance

Tax avoidance means preventing or reducing one's tax liability through manipulations within the framework of existing tax legislation. Tax avoidance, as against tax evasion, is legally permissible and hence a legitimate aim of taxpayers.

Tax avoidance is resorted to through such devices as formation of holding companies to claim artificial deductions, constitution of trusts and family partnerships, transfer of income earning assets to one's wife and children for fractioning income for tax purposes, investing in provident funds and life insurance policies, and manipulation of capital gains.

Since tax avoidance has a colour of legality about it, clever taxpayers do their best to avoid or keep down tax payments. This may force the government to raise tax rates, making the less clever assessees bear a disproportionate tax burden.

Tax laws in many countries incorporate anti-tax avoidance provisions under which certain incomes are included in an assessee's total income, though such incomes legally belong to other persons. For example, in India, Sections 60 to 65 of the Income Tax Act, 1961, deal with instances where an assessee may attempt to reduce his tax liability either by transferring his assets in favour of his family members or by arranging his sources of income in such a manner that tax incidence falls on others, whereas benefit of income, directly or indirectly, is derived by the assessee himself. Thus, income arising to the spouse, minor child, son's wife, son's minor child and certain other persons are clubbed with the assessee's income in certain circumstances. In this regard, the Indian income tax law deviates from the general principle that a person can be assessed in respect of his own income.

4.0 Causes of Black Money and Tax Evasion

4.1 Causes of black money

Generation of Black Money through Illegal Activities: The *criminal component* of black money includes a host of illegal activities. Such activities—anti-social in nature—include, *inter alia*, the following:

1. Smuggling of goods.
2. Forgery, embezzlement, counterfeit currency, and other financial frauds (chit funds etc.).
3. Production/trade of contraband goods (e.g. narcotics, illicit liquor and arms).
4. Illegal mining and illegal felling of forests.
5. Hoarding and black marketing of price-controlled goods and services.
6. Theft, robbery, kidnapping and extortion, human trafficking, sexual

exploitation and blackmailing.

7. Bribes to those holding public offices to secure favours: (a) altering land use, (b) regularizing authorized constructions, (c) speed money to circumvent/fast track procedures, and (d) commission to secure government purchase orders.

All above-mentioned activities are illegal and reflect declining social and moral values. These illegal activities are punishable under various Acts of the Central and State Governments which are administered by various law enforcement agencies. Effective implementation of these Acts is the responsibility of both the Central and State Governments. Some of these offences are included in the schedule of the Prevention of Money Laundering Act, 2002.

Generation of Black Money through Legal Activities: Significant amount of black money, however, is generated through legally permissible economic activities. Though lawful, such activities are not disclosed/reported to the public authorities as per provisions of the law, thereby converting such income into black money. The failure to report/disclose such activities/income may be with the objective of evading taxes or avoiding the cost of compliance related to such reporting/disclosure under some other law.

Generally, a high burden of taxation provides a strong temptation to evade taxes. Sometimes the procedural regulations can be such that complying with them may increase the probability of further scrutiny and thereby the incidence of the burden of compliance. Such situations create incentive to conceal one's true state of affairs and thereby remain outside the reported and accounted proportion of one's activities.

With increased globalisation [6] and economic liberalisation, there has been a manifold increase in cross-border transactions. This has also resulted in increased opportunities for sophisticated devices to avoid tax payment using the different tax rules of different countries and use of tax havens. Global trade amongst various arms of multinational companies (MNCs) has also increased substantially and accounts for a significant proportion of global trade. It also means increasing misuse of transfer pricing, leading to estimations that developing countries might be losing significant resources due to transfer pricing manipulation.

One of the difficulties in preventing abuse of such transfer pricing arrangements is the large disparity between resources deployed by these multinationals and those available with tax administrators, particularly of developing countries. This requires enormous reforms for improving the capacity of tax administration and equipping it with the necessary resources to deal with such modern challenges.

4.2 Causes of tax evasion

High Level of Tax Rates: Among the host of causes of tax evasion and hence the generation of black money, the level of tax rates is probably the most crucial. It is widely believed that higher the rate of tax, the greater is the tendency to evade taxes. High tax rates make tax evasion more tempting. Tax evaders readily take greater risks if they know that in the event of success the reward is high. Per contra, it can be expected that low tax rates improve tax compliance and broaden the tax base.

Less Respect for Government and its Laws: Tax evasion is more in countries where there is general apathy on the part of people towards the government and its laws. People will have less respect for tax laws if they perceive the tax system to be unfair in terms of level of taxation (tax-GDP ratio) [7] and/or distribution of tax burden among various classes (i.e. tax equity). [8] Similarly, there can be a feeling among taxpayers that government is indulging in wasteful expenditure (e.g. digging the roads too often), spending excessively on government functionaries, permitting loan waivers, maintaining perpetually sick public undertakings, and granting unnecessary subsidies. Tax evasion by politicians sends wrong signals to the general public that non-compliance is acceptable.

It is necessary to change the attitude of the people towards Government and its laws. In this connection, the Indian Tax Reforms Committee, 1991, observed, "...there is a widespread feeling among the electorate that there is considerable waste in government expenditure, that there is excess staff and that the tail to teeth ratio is unduly high. And with it all, it is generally felt that the public which pays the taxes gets poor service and members of the public are treated often not as masters who pay but as supplicants." (Government of India, Ministry of Finance, 1991)

Lenient Penal Action: Lenient penal action in case violation of law is detected also encourages tax evasion. In general, countries with relatively poor implementation of regulations tend to have a higher share of unaccounted economy, whereas countries with properly implemented regulations and sound deterrence have smaller *black* economies.

Nature of the Economy: The problem of tax evasion in underdeveloped countries is associated with the peculiar characteristics of their economies which, in most cases, are agriculture-based in the sense that a substantial part of national income originates from and the majority of the work force is engaged in agriculture. Moreover, there is widespread illiteracy, lack of accounting practices, limited monetisation and shortage of administrative resources in these countries. A regime of controls, licences, and shortages also breeds tax evasion and black money.

5.0 Consequences of Black Money/Tax Evasion

The nexus between tax evasion and black money and its distortion of the redistributive role of tax policy was noted by India's Seventh Five Year Plan as follows, "With a sizeable proportion of income and wealth evading taxation, the redistributive impact of progressive taxation had been severely blunted. A reduction in the scale of black income generation would improve distribution of income and wealth after taxation. Besides, if the magnitude of tax evasion is significantly reduced, there would be a greater volume of tax revenue, and a greater volume of public expenditure benefiting the poorer section of the population would become possible." (Government of India, Planning Commission, 1985-90)

Black money in social, economic and political space of the country has a debilitating effect on the institutions of governance and conduct of public policy in the country. Governance failure adversely affects the interests of vulnerable and disadvantaged sections of society. The success of an inclusive growth strategy [9] critically depends on the capacity of society to root out the evil of corruption and black money from its very foundations. Undoubtedly, India needs a speedy transition towards a more transparent and result-oriented economic system.

The effects of tax evasion, resulting in black money, on an economy are indeed disastrous. Some of these are listed below:

1. Tax evasion cuts at the very root of the revenue potential of a tax system and therefore hinders the resource mobilisation efforts of a government. Lack of

funds may distort implementation of development plans and force a government to resort to deficit financing in case public expenditure is inelastic.

2. Tax evasion may interfere with the declared economic policies of a government by distorting saving/investment patterns and availability of resources for various sectors of the economy. For instance, government may impose credit restrictions to discourage certain activities (e.g. speculation) but money saved through tax evasion may finance and encourage the same activities.
3. Evasion of tax seriously undermines the equity attribute of a tax system. Honest taxpayers, who are obliged to bear disproportionate tax burden, feel demoralised and tempted to join the tax evaders' camp.
4. Tax evasion leads to the creation of black money which in turn is a menace to the economy in its own way. Tax evasion and black money encourage concentration of economic power in the hands of undesirable groups in the country.
5. Tax evasion eats into the time and energy of tax administration which is obliged to unravel the intricate manipulations of tax dodgers.
6. Tax evasion leads to degradation of social and moral standards. Social abuses like bribery, intimidation, blackmailing, tampering with official records, submitting fake documents etc. all go with tax evasion.

To conclude, with liberalisation of restrictions on cross-border flow of goods and services and relaxation of foreign exchange control, new opportunities have opened up for tax evasion through tax havens, misuse of transfer pricing, and other sophisticated methods. Globalisation has reduced the cost of these sophisticated methods thereby facilitating generation of black money and its transfer across the border. These changes require new strategies to curb black money.

The fight against generation and accumulation of black money is far more complex and prolonged, requiring stronger intervention of the state. It needs a robust legal framework, commensurate administrative set up, and a very strong resolve to fight the menace.

6.0 Methods to Generate Black Money

Black money may be generated through the crude approach of not declaring or reporting the income or the activities leading to it. This is the likely approach in all cases of criminal, illegal, and impermissible activities. The same approach of not declaring or reporting activities and the income generated therefrom may also be followed in cases of failure to comply with regulatory obligations or tax evasion on income from legitimate activities. However, complete evasion or non-compliance may make such incomes vulnerable to detection by authorities and lead to adverse consequences for the generator.

As an alternative, a safer approach for generation of black money is often preferred, involving manipulation of financial records and accounting. Thus, the best way of classifying and understanding the various ways and means adopted by taxpayers for the generation of black money would be the *financial statement approach*. It elaborates different means by which the accounts prepared for reporting and presenting before the authorities are manipulated to misrepresent income, thereby generating income that amounts to black money.

As is well-known, any transaction entered into by the taxpayer must be reported in books of account which are summarized at the end of the year in the form of financial statements. The financial statements basically comprise (a) statement of income and expenditure called *Profit and Loss Account* or *Income and Expenditure Account* and (b) statement of assets and liabilities called *Balance Sheet*.

Different kinds of manipulations of financial statements resulting in tax evasion and the generation of black money are elaborated in the following paragraphs.

6.1 Out of book transactions:

No Books of Account: This is one of the simplest and most widely adopted methods of tax evasion and generation of black money. Transactions that may result in taxation of receipts or income are not entered in the books of account by the taxpayer. The taxpayer either does not maintain books of account or maintains two sets or records partial receipts only. This mode is generally prevalent among the micro and small enterprises and providers of unskilled and semi-skilled services.

Parallel Books of Accounts: This is a practice usually adopted by those who are obliged under the law, or due to business needs, to maintain books of account. In order to evade reporting activities or the income generated from them, they may resort to maintaining two sets of books of account—one for their own consumption with the objective of managing their business and the other one for the regulatory and tax authorities (income tax, excise, VAT). The second set of books of account, which is maintained for the purpose of satisfying the legal and regulatory obligations of reporting to different authorities, may be manipulated by omitting receipts or falsely inflating expenses, for the purpose of evading taxes or other regulatory requirements.

Other methods under this category include (a) unaccounted assets and (b) investments in shares of listed companies through dummy entities.

6.2 Manipulation of Books of Account

When books of accounts are required to be maintained by taxpayers under different laws (e.g. Income Tax Act, 1961, Companies Act, 1956) it may become difficult for these taxpayers to indulge in out of book transactions or to maintain parallel books of accounts. Such parties may resort to manipulation of the books of accounts to evade taxes.

Manipulation of Sales/Receipts: A taxpayer is required to pay taxes on profit or income which is the difference between sale proceeds or receipts and expenditure. Thus, manipulation of sales or receipts is the easiest method of tax evasion. Other innovative devices may include diversion of sales to associated enterprises, which may become more important if such enterprises are located in different tax jurisdictions and thereby may also give rise to issues related to international taxation and transfer pricing.

In the case of dummy associate entity, there can be a plethora of possible arrangements entered into by such entities to aid generation of black money. In its simplest form, the associate entity may not report its activities or income at all. The main entity may show sales to such a dummy associate entity at a lower price, thereby reducing its reported profits.

More complex scenarios can emerge if the dummy associate entity is situated in a low tax jurisdiction having very low tax rates. Thus, the profit of the Indian entity will be transferred to the low tax jurisdiction and money will be accumulated by the taxpayer in the books of accounts of the entity in the low tax jurisdiction.

Under-reporting of production is another means of artificially reducing tax liability. It may be resorted to for the purpose of evading central excise, sales tax, or income tax.

In short, the following means can be applied to manipulate sales/receipts: (a) suppression of sales/receipts, (b) diversion of sales to associated enterprises (dummy or genuine), (c) inter-relation between unaccounted sales and purchases, (d) artificial deferment of revenues and (e) stamping of incorrect price.

Manipulation of Expenses: Since the income on which taxes are payable is arrived at after deducting the expenses of the business from the receipts, manipulation of expenses is a commonly adopted method of tax evasion. The expenses may be manipulated under different heads and result in under-reporting of income. It may involve inflation of expenses, sometimes by obtaining bogus or inflated invoices from the so called *bill masters*, who make bogus vouchers and charge nominal commission for this facility. Sometimes it can also involve *hawala* operators, who operate shell entities in the form of proprietorship firms, partnership firms, companies, and trusts. These operators may accept cheques for payments claimed as expense and return cash after charging some commission.

There have been instances of claims of bogus expenses to foreign entities. The payments can be shown to foreign entities in the form of advertisement and marketing expenses or commission for purchases or sales. The funds may be remitted to the account of the foreign taxpayer and the money can either be withdrawn in cash or remitted back to India in the form of non-taxable receipts. Such money may also be accumulated in the form of unaccounted assets of the Indian taxpayer abroad.

Besides inflation of purchase/raw material cost, expenses like labour charges, entertainment expenses, and commission can be inflated or falsely booked to reduce profits.

Manipulation of Capital: The balance sheet of the taxpayer contains details of assets, liabilities, and capital. The capital of the taxpayer is the accumulated wealth which is invested in the form of assets or as working capital of the business. Manipulation of capital can be one of the ways of laundering black money and introducing it in the books of accounts. Manipulation of capital can take place, *inter alia*, through following means: (a) shares at high premium, (b) bogus gifts, and (c) bogus capital gains and purchase of bogus losses.

Manipulation of Closing Stock: Suppression of closing stock both in terms of quality and value is one of the most common methods of understating profit. Refiner versions of such practice may include omission of goods in transit paid for and debited to purchases, or omission of goods sent to the customer for approval. A more common approach is undervaluation of inventory (stock of unsold goods), which means that while the expenses are being accounted for in the books, the value being added is not accounted for, thereby artificially reducing the profits.

Manipulation of Capital Expenses: Over-invoicing plant and equipment or any capital asset is an approach adopted to claim higher depreciation and thereby reduce the profit of the business. Increase in capital can also be a means of enabling the businessman to borrow more funds from banks or raise capital from the market. It has been seen that such measures are sometimes resorted to at the time of bringing out a capital issue.

International Transactions through Associate Enterprises: Another way of manipulating accounted profits and taxes payable thereon may involve using associated enterprises in low tax jurisdictions through which goods or other material may be passed on to the concern. Inter-corporate transactions between these associate enterprises belonging to the same group or owned and controlled by the same set of parties may be arranged and manipulated in a way that leads to evasion of taxes. This can often be achieved by arrangements that shift taxable income to the low tax jurisdictions or tax havens, and may lead to accumulation of black money earned from within India to another country.

7.0 Devices Adopted to Evade Taxes

7.1 Income tax

Income tax is evaded through non-reporting, under-reporting and misreporting of income (e.g. showing non-agricultural income as agricultural income) [10]

The following devices are generally employed to evade income tax:

1. Non-reporting/under-reporting of taxable income.
2. Maintaining multiple set of account books, fraudulent changes in account books, and keeping transactions out of account books.
3. Opening and operating bank accounts under assumed names.
4. Doing business in the name of dummies.
5. Over-reporting expenses.
6. Fragmenting income to reduce tax liability.
7. Under-invoicing sales and other transfer pricing manipulations.

7.2 Excise Duties

Excise evasion is generally resorted to by adopting, *inter alia*, following malpractices.

1. Incorrect accountal of goods.
2. Undervaluation of goods.
3. Flouting the conditions subject to which any goods may be exempted from duty.

7.3 Value-Added Tax (VAT)

The proponents of VAT claim that evasion under it is difficult and minimal. The tax credit method ensures cross-checking of the records of taxpayers through invoices. Buyer firms insist on supplier firms to furnish invoices which help the former to claim tax credit. Since tax liability of a single taxpayer under VAT is only a fraction of the total amount of tax, the incentive for evasion is relatively weak. Even a successful evasion would mean less revenue loss as compared to the one suffered under a system of turnover tax on gross value (excise duty or sales tax).

Despite the self-policing nature of VAT, opportunities do exist under it for evasion and fraud. In fact, VAT provides opportunities for fraud (fictitious claims for refunds) which are not available under other forms of commodity taxation. The methods commonly applied to defraud tax authorities under VAT include, *inter alia*, the following.

1. Use of fake invoices to claim tax credit.
2. Tax credit claims on purchases for personal use.
3. Over-reporting of sales of zero-rated goods.

4. Secret deals between buyers and sellers as regards issuance of receipts.
5. Formation of fake companies which sell receipts to traders to enable them to claim tax credit on inputs.

Thus, VAT is as susceptible to evasion and fraud as any other tax. An efficient tax machinery capable of cross-checking a large number of invoices through an elaborate computer system is a pre-requisite for the successful implementation of VAT.

7.4 Customs duties

Evasion of customs duties takes place through following malpractices.

1. Invoice misclassification.
2. Manipulation of documents.
3. Suppression of quantities imported.

8.0 Estimates of Black Money/Tax Evasion

Since black money is unaccounted for, there are no reliable estimates of it. Similarly, there is no well-defined and universally acceptable methodology for estimation of black money. Hence, all attempts at its estimation have produced results with wide variations. Several estimates have been floated—often without adequate factual basis—on the magnitude of black money generated in the country and the unaccounted wealth stashed aboard.

Widespread tax evasion is a perennial problem of the Indian tax system. The history of taxation law amendments in India is essentially a history of plugging loopholes, as and when discovered, to prevent leakages of revenue. It is noteworthy that tax evasion is not confined to income tax only, rather it is widely practised for other direct taxes also like wealth tax. The ridiculously low yield from these taxes is partly due to plethora of exemptions/concessions and also due to widespread evasion. In India, economic inequalities have been caused mainly by the inequitable ownership of wealth and the failure of the wealth tax to make a headway in lessening inequalities is indeed regrettable.

It may be recalled that in 1957 and 1958, three new taxes were introduced, viz. wealth tax, expenditure tax, and gift tax. Estate duty was already in operation since 1953. The basic philosophy underlying the introduction of the system of integrated direct taxes was to prevent evasion and avoidance of direct taxes and thereby to reduce inequalities of income and wealth. However, the yield from wealth tax, expenditure tax, gift tax, and estate duty has never been of much significance in the Central tax structure. The meagre revenue collection ultimately led to the abolition of expenditure tax, estate duty and gift tax in 1966, 1985 and 1998 respectively. Wealth tax continues to be in operation.

As regards black money stashed abroad, the White Paper on Black Money observed, "It is however useful to mention here one estimate of the amount of Indian deposits in Swiss banks (located in Switzerland) which has been made by the Swiss National Bank. Its spokesperson stated that at the end of 2010, the total liabilities of Swiss Banks towards Indians were 1.945 billion Swiss Francs (about Rs. 9,295 crore). The Swiss Ministry of External Affairs confirmed these figures when a reference was made by the Indian Ministry of External Affairs to them." (Government of India, Ministry of Finance, 2012, para 2.6.4) The White Paper further noted, “The illicit money transferred outside India may come back to India through various methods such as hawala, mispricing, foreign direct investment (FDI) through beneficial tax jurisdictions, raising of capital by Indian companies through global depository receipts (GDRs), and investment in Indian stock markets through participatory notes. It is possible that a large amount of money transferred outside India might actually have returned through these means.” (Government of India, Ministry of Finance, 2012, para 2.4.9)

9.0 Measures Adopted to Curb Black Money/Tax Evasion

Direct Taxes Enquiry Committee (Chairman: Justice K.N. Wanchoo), 1971, had suggested various measures to fight the evil of black money and tax evasion. Some of the measures suggested were as follows.

1. Reduction in tax rates.
2. Minimisation of controls and licences.
3. Regulation of donations to political parties.
4. Creating confidence among small taxpayers.
5. Substitution of sales tax by excise duty.
6. Vigorous prosecution policy.
7. Compulsory maintenance of accounts.

To give effect to the recommendations made by the Committee, the Government enacted the Taxation Laws (Amendment) Act, l975. This Act, *inter alia*, provided stringent punishment for tax evaders. In cases where tax evasion exceeded Rs. l lakh or prosecution was for the second or subsequent offence, the maximum punishment prescribed was 7 years rigorous imprisonment. Also, the discretionary powers to courts to award monetary punishment as an alternative to imprisonment or to reduce the term of imprisonment less than the minimum period, was withdrawn.

Efforts have been made to curb tax evasion and control black money through various measures: Some of these are described below.

1. Lowering of tax rates.
2. Tax amnesties.
3. Advance tax payment.
4. Withholding tax [or tax deduction at source (TDS)].
5. Presumptive tax for small traders.
6. Permanent Account Number (PAN) or General Index Register Number (GIR).
7. Survey of income tax.
8. Summons, and search and seizure.
9. Restrictions on the transfer of high value immovable properties
10. Penalties and prosecutions.

9.1 Lowering of tax rates

The Report of the Direct Taxes Enquiry Committee (DTEC), 1971, was a milestone in the area of income tax rates. The Committee made a number of far-reaching suggestions for unearthing black money, preventing evasion and avoidance of taxes, and reducing arrears. One important recommendation of the Committee related to reduction in the rates of direct taxes which in its view were mainly responsible for tax evasion because they made tax evasion profitable and attractive. The rates of individual income tax were quite high till the year 1973-74. These high rates, necessitated by contingencies like drought and war, when combined with the prevailing shortages, resulted in controls and licences, and thereby provided further incentives for evasion of taxes. It was largely in this economic environment that generation of black money became highly prevalent and acquired serious proportions.

However, pursuant to the recommendations of the DTEC, the Government initiated a series of rate reductions in individual income tax. The top marginal rate of tax was reduced from 97.7 per cent in 1973-74 to 77 per cent in 1974-75, and further down to 66 per cent in 1976-77. It is noteworthy that DTEC had recommended a maximum marginal rate of 75 per cent. (Government of India, Ministry of Finance, 1971)

The downward trend in the rate of income tax was temporarily reversed during the brief Janata Government rule at the Centre. The top marginal rate of income tax was increased from 66 per cent in 1976-77 to 69 per cent in 1977-78, and further up to 72 per cent in 1979-80. However, the policy of low direct tax rates started by the Congress Government in 1974 and carried forward in 1976 was further reinforced after it came back to power at the Centre in 1980. After a series of revisions, the maximum marginal rate of individual income tax was 54 per cent (including employment surcharge of 8 per cent), applicable from the financial year 1990-91.

Consequent upon the recommendations contained in the Interim Report of the Tax Reforms Committee (Chairman: Raja Chelliah), 1991, the top marginal rate was fixed at 44.8 per cent (including surcharge) from the financial year 1992-93. The Finance Act, 1994 abolished the surcharge of 12 per cent and hence the maximum marginal rate of tax was 40 per cent from the financial year 1994-95. From the same year it was made applicable on incomes over Rs. 1,20,000. It may be recalled that the top marginal rate of income tax applied to incomes above Rs. 1 lakh from 1967-68 to 1993-94. The Rs. 1 lakh of 1967-68 was approximately equivalent to Rs. 5.5 lakh of 1993-94. This showed the laxity of the administration in adjusting tax brackets for inflation. It is noteworthy that Tax Reforms Committee had recommended 40 per cent maximum rate inclusive of surcharge for income exceeding Rs. 2 lakh.

The maximum marginal rate of personal income tax was further reduced from 40 per cent to 30 per cent in the 1997-98 budget. In another significant move, it was made applicable to incomes above Rs. 1,50,000.

Low tax rates are welcome provided they improve compliance and revenue yield. However, to expect that lowering of rates would improve compliance automatically is unrealistic because tax evasion occurs at all levels of income. As the Indian Direct Taxation Administration Enquiry Committee, 1958-59, observed, "While we cannot deny that the higher the rate of tax, the greater will be the temptation for evasion and avoidance, we feel that the tax rates by themselves are not to blame for the large extent of evasion in the country. Even if the rates of tax are reduced, evasion will still continue, because it exists at all levels of income." (Government of India, Ministry of Finance, 1958-59)

9.2 Tax amnesties

Government may provide opportunity, from time to time, to tax evaders to declare their past concealments of income and wealth without fear of being prosecuted. Tax amnesty (or impunity) is granted only for the past in order to secure better compliance and thus higher tax yield in the present and future. Tax amnesties (or voluntary disclosure schemes) bring concealed money in the open, broaden the base of investment and hence accelerate economic development.

However, tax amnesties are criticized on the grounds that they provide a premium on dishonesty and are unfair to honest taxpayers. Tax amnesties set bad precedents and encourage tax evaders in the hope that they will be let off leniently for their past sins any time in the future. Practically, the same group of tax evaders takes advantage of tax amnesties announced by the government. The honest taxpayers are demoralised and the tax enforcement machinery also loses respect in the eyes of the common man.

In India, tax amnesties with varied characteristics have been offered from time to time to unearth black money. These amnesties provided taxpayers immunity from interest, penalty, investigation or prosecution in exchange for disclosures of incomes which did not pay tax.

9.3 Advance tax payment

Though the regular assessment in respect of any income is made in a later assessment year, the tax on such income is payable by way of advance payment or deduction at source. Section 208 of the Income Tax Act, 1961 makes it obligatory to pay advance tax in every case where the advance tax payable is Rs. 10,000 or more.

9.4 Withholding tax [or Tax Deduction at Source (TDS)]

There are provisions under various sections of the Act regarding tax deduction at source (TDS) [11], e.g. deduction of tax from salaries (Section 192). Other incomes covered under the scheme of TDS include fees for professional or technical services, interest, rent from real estate, commission from insurance, sale of lottery tickets, and winnings from lotteries, crossword puzzles and horse racing.

In recent years, improvement in the per centage share of direct taxes (mainly income tax) has taken place due to widening of the tax base, presumptive taxation and broadening the scope of TDS. In this context, the Ninth Five Year Plan (1997-2002) observed, "The share of TDS in gross collection of income tax increased from about 23 per cent in 1980-81 to about 37 per cent in 1989-90, but declined subsequently to about 31 per cent in 1994-95. One of the major loopholes which contributes to the decline in revenue from TDS relates to the branch-wise threshold of Rs. 10,000 for the purpose of deducting income tax at source from interest on time deposits with banks. Further, the provision for TDS does not apply to non-banking financial companies. Other deficiencies from which the TDS scheme suffers arise from lack of proper monitoring and scrutiny." (Government of India, Planning Commission, 1997-2002)

9.5 Presumptive tax for small traders [12]

In its Interim Report, submitted in December 1991, the Tax Reforms Committee examined the problems and possibilities of taxing the small business sector. The Committee suggested two new presumptive taxes on small businesses:

1. A fixed tax on businesses whose turnover was less than Rs. 5 lakh.
2. An estimated income scheme on small businesses with a turnover above Rs. 5 lakh but less than Rs. 25 lakh.

The schemes envisaged profit to be a certain per centage of turnover depending on the type of activity from which it was earned. The Government introduced the first scheme through the Finance Act, 1992, but deferred its decision to introduce the second scheme.

The presumptive tax system for persons engaged in retail trade with an annual turnover up to Rs. 5 lakh was introduced on an experimental basis. The scheme was in operation initially for two assessment years 1993-94 and 1994-95. It was continued after the expiry of these two years. The objective of the new simplified procedure for taxation was to widen the tax base by encouraging shopkeepers (including those engaged in vocations like tailoring, typewriting, photocopying, repair work etc.) and other small retail traders to pay taxes. The scheme had the following features: The scheme was optional and open to individuals not assessed to tax earlier and who had an income from the business of retail trade having an annual turnover up to Rs. 5 lakh. Persons opting for the scheme were deemed to have a turnover of Rs. 5 lakh and their total income was deemed to be Rs. 35,000 (Rs. 37,000 for A.Y. 1994-95) on which the tax worked out to Rs. 1,400 after allowing for the basic exemption of Rs. 28,000 (Rs. 30,000 for A.Y. 1994-95). A retail trader opting for the scheme had only to file the simplified statement (name, address, nature of business etc.) and pay a tax of Rs. 1,400 by 15th March of the financial year in which the income was earned. The scheme was optional to avoid objection on constitutional grounds. If presumptive tax results in a higher tax burden than the one on the basis of book profit, it can be said to violate Article 14 of the Constitution which guarantees equality before law. Thus, the taxpayer had the option to pay presumptive tax or ask for regular assessment of his income, whichever he thought was advantageous to him.

Unfortunately, the scheme of presumptive taxation did not gain popularity with small traders and self-employed entrepreneurs. In 1992-93, the first year of the operation of the scheme, 1,16,644 persons opted for the scheme and paid a total tax of Rs. 16.4 crore, as against the anticipated revenue collection of Rs. 140 crore. (Government of India, *Economic Survey*, 1993-94) This was by no means a significant addition to the existing 70 lakh individual assessees under the income tax net. The number of shopkeepers and other small traders was much higher. The scheme touched only the tip of the iceberg.

The Government introduced through the Finance Act, 1994 two new schemes, viz. Sections 44AD and Sections 44AE, to provide for a method of estimating income from the business of civil construction and plying or hiring of trucks respectively. The scope of Section 44AD has been enlarged and it is now applicable to any business except plying, hiring, or leasing goods carriage referred to under section 44AE. While section 44AD applies to all assessees whose gross receipts from the business do not exceed Rs. 1 crore, section 44AE applies to assessees owning not more than 10 trucks at any time during the previous year. Under Section 44AD, the income from these businesses (mentioned above) is estimated at 8 per cent of the gross receipts paid or payable to an assessee. Income of truck owners is assessed at Rs. 5,000 per month per heavy goods vehicle and at Rs. 4,500 per month per medium and light vehicle.

In the 1997-98 budget, the Finance Minister discontinued the presumptive scheme under Section 115K as it failed to yield the desired results. In its place, he introduced a new estimated income scheme for retail traders (Sec. 44AF). The new scheme was applicable to persons engaged in the business of retail trade of any goods or merchandise having a total turnover of less than Rs. 40 lakh. The income of the trader was estimated at 5 per cent of the total turnover. However, with effect from AY 2011-12, sec 44AF has been discontinued.

9.6 Permanent Account Number (PAN) or General Index Register Number (GIR): In order to strengthen the efforts at enforcement, the Finance Minister in his 1998-99 budget made it obligatory for assessees to quote their PAN or GIR mandatorily in respect of the following high value transactions: purchase and sale of immovable property; purchase and sale of motor vehicles; transactions in shares exceeding Rs. 10 lakh; opening of new bank accounts; fixed deposits of more than Rs. 50,000; applications for allotment of telephone connections; and payments to hotels exceeding Rs. 25,000.

10.0 Recent Legislative Measures to Prevent Generation of Black Money

A number of proactive steps have recently been taken in order to create an appropriate legislative framework for preventing the generation of black money and for its detection.

10.1 Prevention of Money Laundering Act (PMLA), 2002

PMLA was enacted to prevent money laundering and provide for confiscation of property derived from, or involved in, money laundering and for matters connected therewith or incidental thereto. The Act also addresses international obligations under the Political Declaration and Global Programme of Action adopted by the General Assembly of the United Nations to prevent money laundering.

To strengthen the provisions of the PMLA, amendments were carried out in 2009. These amendments have introduced new definitions to clarify and strengthen the Act and strengthened provisions related to attachment of property involved in money laundering and its seizure and confiscation. More offences have been added in Parts A and B of the Schedule to the Act, including those pertaining to insider trading and market manipulation as well as smuggling of antiques, terrorism funding, human trafficking other than prostitution, and a wider range of environmental crimes. A new category of offences with cross-border implications has been introduced as Part C.

The problem of black money is no longer restricted to the geo-political boundaries of any country. It has become a global menace that cannot be contained by any nation alone. In view of this, India has become a member of the Financial Action Task Force (FATF) [13] and Asia/Pacific Group on Money Laundering (APG) [14} which are committed to the effective implementation and enforcement of internationally accepted standards against money laundering and the financing of terrorism. Consequent to the submission of an action plan to the FATF for bringing India's anti-money laundering legislation on par with international standards and to address some of the deficiencies of the Act that have been experienced by the implementing agencies, PMLA 2002 is further proposed to be amended through the Prevention of Money Laundering (Amendment) Bill 2011, which is under consideration of Parliament. The Bill seeks to introduce the concept of *corresponding law* to link the provisions of Indian law with the laws of foreign countries and provide for transfer of the proceeds of the foreign predicate offence in any manner in India. It also proposes to enlarge the definition of the offence of money laundering to include therein activities like concealment, acquisition, possession, and use of proceeds of crime as criminal activities and remove the existing limit of Rs. five lakh for imposition of fine under the Act.

It also strengthens provisions for attachment and confiscation of the proceeds of crime and widens the investigative powers of the concerned officials and clubs offences listed under Schedules A and B into a single Schedule.

10.2 Benami Transaction (Prohibition) Bill 2011

This comprehensive legislation was introduced in the Lok Sabha on August 18, 2011 and is currently being examined by the Standing Committee on Finance. It will iron out the infirmities in the Benami Transaction (Prohibition) Act enacted in 1988 and formalise the procedure for implementing the benami law, including the procedure for determination, confiscation, prosecution, and miscellaneous requirements.

This Bill defines benami property and a benami transaction in terms of a transaction or agreement where a property is transferred to or held by a person for a consideration provided or paid by another person. Such a property is held for the immediate or future benefit, direct or indirect, of the person providing the consideration. A transaction or arrangement in respect of a property carried out or made in a fictitious name or where the owner of the property is not aware of or denies knowledge of such ownership is also included in the definition of benami transaction. The Bill specifies the consequences of benami transactions in the form of confiscation of the benami property and imprisonment up to 2 years in addition to a fine. This Bill also provides the procedure for enquiry and determination of benami property and its consequences as well as the authorities empowered to act for this purpose, including the appellate authorities. After the report of the Standing Committee is received, the Benami Transactions (Prohibition) Bill 2011 will be moved for passage in Parliament and the relevant rules notified thereafter.

10.3 Public Procurement Bill

The Public Procurement Bill 2012 was approved by the Union Cabinet on April 12, 2012 for introduction in Parliament. The Bill seeks to regulate procurement by ministries/departments of the Central Government and its attached/subordinate offices, Central public sector enterprises (CPSEs), autonomous and statutory bodies controlled by the Central Government and other procuring entities with the objectives of ensuring transparency, accountability and probity in the procurement process, fair and equitable treatment of bidders, promoting competition, enhancing efficiency and economy, safeguarding integrity in the procurement process, and enhancing public confidence in public procurement.

The Bill is based on broad principles and envisages a set of detailed rules, guidelines, and model documents. It builds on national and international experience and best practices as appropriate for the needs of the Government of India. It will create a statutory framework for public procurement which will provide greater accountability, transparency, and enforceability of the regulatory framework. The Bill codifies the essential principles governing procurement required for achieving economy, efficiency, and quality as well as combating corruption. It legally obligates procuring entities and their officials to comply with these principles. It also ensures that competition will be maximised in procurement, while providing for adequate flexibility for different types of procurement needs. It puts in place a strong framework of transparency and accountability through a public procurement portal and a grievance redressal system in which an independent mechanism, chaired by a retired High Court Judge, will review grievances.

10.4 Prevention of Bribery of Foreign Public Officials and Officials of the Public International Organisations Bill 2011

This Bill was introduced in the Lok Sabha on March 25, 2011 and is under consideration of the Standing Committee. The Bill seeks to prevent corruption relating to bribery of foreign public officials and officials of public international organisations and to address matters connected therewith or incidental thereto. The proposed legislation prohibits acceptance of gratification by foreign public officials or officials of public international organisations as well as the act of giving such gratification or its abetment. The bill also empowers the Central Government to enter into agreements with foreign countries for enforcing the provisions, makes offences under the proposed act extraditable, and provides for attachment, seizure and confiscation of property in India or the respective country and mutual assistance in this regard.

10.5 Lokpal and Lokayukta Bill, 2011

After being passed by the Lok Sabha, it is now under consideration of the Rajya Sabha. It provides for the establishment of the institution of Lokpal to inquire into allegations of corruption against certain public functionaries and for matters connected therewith or incidental thereto. The Bill envisages setting up of the institution of Lokpal consisting of a chairperson and 8 members with the stipulation that half of the members shall be judicial members. It shall have its own Investigation Wing and Prosecution Wing with such officers and staff as are necessary to carry out its functions. The Lokpal shall inquire into allegations of corruption made in respect of the following:

Prime Minister after he has demitted office.

A Minister of the Union.

A Member of Parliament.

Any Group 'A' officer or equivalent.

Chairperson or member or officer equivalent to Group 'A' in any body/board/corporation/authority/company/society/ trust/ autonomous body established by an Act of Parliament or wholly or partly financed or controlled by the Central Government.

Any director, manager, secretary or other officer of a society or association of persons or trust wholly or partly financed or aided by the government or in receipt of any donations from the public and whose annual income exceeds such amount as the Central Government may by notification specify.

However, organisations created for religious purposes and receiving public donations shall be outside the purview of the Lokpal. The Lokpal shall not require sanction or approval under Section 197 of the Code of Criminal Procedure 1973 or Section 19 of the Prevention of Corruption Act 1988 in cases where prosecution is proposed. The Lokpal shall also have powers to attach the property of corrupt public servants acquired through corrupt means.

10.6 Citizens' Grievance Redressal Bill

The Right of Citizens for Time Bound Delivery of Goods and Services and Redressal of their Grievances Bill, 2011, which is presently under consideration of the Lok Sabha outlines the responsibilities of government departments towards citizens and how someone who is denied the service due to him can seek redressel. It mandates that every public authority or government department has to publish a citizen's charter listing all services rendered by that department along with a grievance redressal mechanism for non-compliance with the citizen's charter. It also sets up a Central Public Grievances Redressal Commission, with an equivalent in every state, and provides for a designated authority from a department other than the one against which the complaint has been filed to address the complaint. The other features of the Bill are as under:

1. The Citizen's charter has to clearly explain the complaint redressal system for that office, like which officer in that department the complaint should be registered with.
2. Every government department or public authority shall create an *information and facilitation centre* that could include a customer helpline or help desk to deliver services and handle complaints.
3. Every public authority will appoint or designate Grievance Redressal Officers whose contact information will be clearly shared with the public. The Grievance Redressal Officer shall provide the public with all necessary assistance in filing complaints. Within two days of the complaint being registered, the citizen who has filed a complaint will receive—by SMS or mail—a unique complaint number and a time frame within which the complaint will be handled. That time frame cannot exceed 30 days from when the complaint was received.
4. The Grievance Redressal Officer has to ensure that the person who made the complaint is informed in writing with an Action Taken Report on how his/ her complaint was handled. If this does not happen, the citizen can appeal to a designated authority. This officer can summon others and ask them to testify under oath.
5. The designated authority has to ensure that the appeal is acted upon within 30 days. It can fine the officer concerned and compensate the citizen, if appropriate.
6. If a citizen is not happy with the designated authority's response or decision, he can take his complaint to the State Public Grievance Redressal Commission (assuming that the complaint is against a government department that is under the jurisdiction of a state government). Each state shall set up this body. It will have a Chief Commissioner and a maximum of ten other commissioners. They will be appointed by a committee consisting of the Chief Minister, the leader of opposition in that state, and a sitting judge of the High Court. The commissioners will have a term of five years.
7. For citizens who are unhappy with a service provided to them from a government office that is under the jurisdiction of the Central Government,

they can finally appeal to the Central Public Grievance Redressal Commission. This body will have a Chief Commissioner and a maximum of ten commissioners who will be appointed by the President after they are chosen by a committee comprising the Prime Minister, the leader of opposition, and a sitting judge of the Supreme Court.

8. If citizens are unhappy with the decision of the Central or State Commissions, they can appeal to the Lokayukta or Lokpal.

10.7 Judicial Standards and Accountability Bill, 2010

It was passed by the Lok Sabha and is under consideration of the Rajya Sabha. The Bill provides a mechanism for enquiring into complaints against judges of the Supreme Court and High Courts, lays down judicial standards, and requires judges of the Supreme Court and High Courts to declare their assets and liabilities. The Bill seeks to replace the Judges (Inquiry) Act 1968 while retaining its basic features. The enactment of the Bill will address the growing concerns regarding the need to ensure greater accountability of the higher judiciary by bringing in more transparency and will further strengthen the credibility and independence of the judiciary. The Bill seeks to lay down enforceable standards of conduct for judges. The main features of the Bill are as under:

1. It requires judges to declare their assets, lays down judicial standards, and establishes processes for removal of judges of the Supreme Court and High Courts.
2. It requires judges to declare their assets and liabilities and also those of their spouses and children.
3. The Bill establishes the National Judicial Oversight Committee, the Complaints Scrutiny Panel, and an investigation committee. Any person can make a complaint against a judge to the Oversight Committee on grounds of *misbehaviour*.
4. A motion for removal of a judge on grounds of misbehaviour can also be moved in Parliament. Such a motion will be referred for further inquiry to the Oversight Committee.
5. Complaints and inquiries against judges will be confidential and frivolous complaints will be penalised.
6. The Oversight Committee may issue advisories or warnings to judges and

also recommend their removal to the President.

10.8 Public Interest Disclosure and Protection to Persons Making the Disclosure Bill, 2010

Commonly known as the Whistleblowers' Bill, it was passed by the Lok Sabha and is under consideration of the Rajya Sabha. The Bill seeks to provide *adequate protection to persons reporting corruption or wilful misuse of discretion which causes demonstrable loss to the government or commission of a criminal offence by a public servant*. While the measure sets out the procedure to inquire into disclosures and provides adequate safeguards against victimisation of the whistleblower, it also seeks to provide punishment for false or frivolous complaints.

11.0 Conclusion

To sum up, prevention and control of black money generation is a pre-requisite to establish an equitable, transparent and a more efficient economy. The factors leading to generation of black money in India —along with the various measures attempted to counter it—make it clear that there is no single remedy to curb, control, and finally prevent the generation of black money. In fact, a comprehensive mix of well-defined strategies is needed by the Central and State Governments and put into practice by all their agencies in a co-ordinated manner.

The fight against the menace of black money has to be at ethical, socio-economic and administrative levels. At the ethical level, we have to reinforce value/moral education in the school curriculum and build good character citizens, particularly highlighting the ills of tax evasion and black money. At the socio-economic level, the thrust of public policy should be to discourage conspicuous and wasteful consumption/expenditure, encourage savings, frugality and simplicity, and reduce the gap between the rich and the poor.

End Notes

1. Under entry 63 of List II (State List) in the Seventh Schedule of the Constitution of India, stamp duty is levied by the State Governments on the registration of property or other

conveyances. Till recently, the stamp duty rates were quite high in most states and the procedures for evaluating the conveyances were also complicated. In this context, the Tenth Five Year Plan (2002-07) remarked, "Stamp duty needs to be paid on all documents which are registered and the rate varies from state to state. With stamp duty rates of 13 per cent in Delhi, 14.5 per cent in Uttar Pradesh and 12.5 per cent in Haryana, India has perhaps one of the highest levels of stamp duty. Some states even have double stamp incidence, first on land and then on its development. In contrast the maximum rate levied in most developed markets whether in Singapore or Europe is in the range of 1-2 per cent. Even the National Housing and Habitat Policy, 1998, recommended a stamp duty rate of 2-3 per cent. Most of the methods to avoid registration are basically to avoid payment of high stamp duty.

Another fall out of high stamp duty rates is the understatement of the proceeds of a sale. This is also linked to payment of income tax and capital gains tax. When registration has not been effected, a transfer is not deemed to have taken place and hence capital gains tax can be totally avoided. Thus, the present provisions in various laws and their poor implementation have led to a situation where there is considerable financial loss to the exchequer on account of understatement of sale proceeds, non-registration and consequent non-payment of stamp duty and avoidance of capital gains tax." [Government of India, Planning Commission, *Tenth Five Year Plan* (2002-07), Volume II, pp. 833-834.]

Of late, states have undertaken reforms by reducing the duty rates and streamlining procedures for evaluation of property. After the reduction of rates, the general experience has been revenue-augmentation due to improved compliance of law.

2. Derivative in mathematics means a variable derived from another variable. The term *derivative* indicates that it has no independent value, i.e. its value is entirely *derived* from the value of the underlying asset. The underlying asset can be security, commodity, bullion, currency, live stock or anything else. In other words, derivative means a forward, future, option or any other hybrid contract of pre-determined fixed duration, linked for the purpose of contract fulfilment to the value of a specified real or financial asset of an index of securities. Similarly, in the financial sense, a derivative is a financial product, which has been derived from a market for another product. Without the underlying product, derivatives do not have any independent existence in the market.

   Derivative instruments are defined by the Indian Securities Contracts (Regulation) Act, 1956 to include (1) a security derived from a debt instrument, share, secured/unsecured loan, risk instrument or contract for differences, or any other form of security and (2) a contract that derives its value from the prices/index of prices of underlying securities.
3. A participatory note (PN) is a derivative instrument issued in foreign jurisdictions, by a foreign institutional investor (FII)/or one of its associates, against underlying Indian securities.
4. National Commission for Enterprises in the Unorganized Sector [NCEUS] (Chairman: Arjun Sengupta), was set up by the Government of India on September 20, 2004, to "review the status of unorganized/informal sector in India including the nature of enterprises, their size,

spread and scope, and magnitude of employment," This step was taken to ensure the welfare and well-being of all workers, particularly those in the unorganized sector, who constitute more than 93 per cent of workforce. NCEUS prepared and submitted to the Government a number of reports before submitting its final report in 2009.

5. Transfer pricing refers to the price attached to transactions between the divisions (e.g. branches or subsidiaries) of a company. Transfer pricing is usually considered in a global context, particularly in relation to cross-frontier transactions within a multinational company.
6. Globalisation implies widening and deepening integration with the *globe*, i.e. with people and processes abroad. The trend towards the evolution of a global society is generally thought of in economic terms and in terms of the consequences of the revolution in communication technologies. There is undoubtedly much greater economic integration among the nations of the world today. Globalisation is widely seen as the most important factor that could influence economies of nations the world over in the new millennium. The rapid advancement in information technology and communications has made it not just possible but absolutely essential for economies of the world to adapt or fall by the wayside.
7. Level of taxation in a country is traditionally judged in terms of the ratio which taxes bear to some measure of national income. This ratio is called tax-GDP ratio and the change in it is determined by variations in both the numerator (total tax revenue) and the denominator (national income).
8. Tax equity refers to *fair* or *just* or *equitable* distribution of tax burden among taxpayers. Though fairness and justness in taxation are universally accepted, these terms are rarely defined rigorously and can be interpreted in various ways. Hence, there is no unanimity of opinion as to the type of tax system which results in the most equitable distribution of tax burden.

   There are two main approaches to tax equity in tax literature: the Benefit Principle of Taxation which states that tax payments should be proportional to the benefits derived from government services, and the Ability-to-Pay Principle of Taxation which holds that each taxpayer should contribute to the public exchequer in line with his ability-to-pay.
9. Inclusive growth may be defined as growth that promotes equal opportunities and increases access to these opportunities, i.e. growth that allows all members of society to participate in and contribute equally to development efforts, regardless of individual circumstances. This concept appears in Asian Development Bank’s (ADB) *Strategy 2020* that examines the extent of inequality of opportunities and to what extent it can be overcome by different types of growth process. The main idea in the ADB’s approach is to focus on productive employment as an important element of inclusive growth.

   Inclusive growth, defined in a broader sense has three dimensions: (1) Equity among all sections of the society. (2) Equity among all sectors of the economy. (3) Equity among all regions in the country.

   Thus, inclusive growth means inter-group, inter-sector as well as inter-regional equity. Growth is inclusive when it creates economic opportunities along with ensuring equal access to them.

10. Agricultural income is exempt from tax under section 10 (1) of the Income Tax Act, 1961.
11. TDS is a system of collecting income tax whereby money is periodically deducted by the employers, financial institutions, and others from wages of employees, returns on securities, and other payments. Thus, intermediaries (or third parties) do the job on behalf of the government as regards assessment of the taxable base and the collection of tax thereon. Generally, a fixed per centage is withheld from the payment made and the same is deposited in government's account. At the time of filing the return of income, the taxpayer encloses withholding tax receipts and in case of overpayment he can claim refund of tax. Tax withholding system (also called tax deduction at source or Pay-As-You-Earn) satisfies the canon of convenience both for the fiscal authorities and the taxpayers. It is beneficial for the government because it reduces the possibility of tax evasion, ensures prompt tax payment, and simplifies tax collection. It does not allow any lag between the time of receiving income and the time of tax payment. For the taxpayer, it is an instalment plan of taxation and hence convenient. However, tax withholding involves additional paper work on the part of tax deductors. It also adds to the burden of taxpayers who have to obtain tax deduction certificates from deductors, fill additional tax forms, and wait for refunds.
12. Presumptive Tax: In every country, there are some soft-to-tax and hard-to-tax sources of income. Wages and salaries are properly recorded and therefore it is easy to assess and collect taxes on them through the Pay-As-You-Earn (PAYE) system. Similarly, income from securities paid through banks can easily be subjected to deduction at source.

    Contrarily, the three hard-to-tax classes of the non-corporate sector are: (a) unincorporated commercial and industrial units, (b) self-employed professionals, and (c) rich peasantry. The problem of taxing the first two categories relates to accounting difficulties while in the case of third category, it is essentially the lack of political will. Non-reporting and under-reporting of income is quite sizeable in these sectors. The growing small business sector is a tax haven. It is very difficult to enforce a reliable system of book-keeping to assess earnings of this sector. Pragmatically, a system of lump sum taxation may be tried in place of taxation of profits. Presumptive tax relates to the use of appropriate indicators of income, wealth etc. instead of the actual records of these tax bases. In the case of income tax, a presumptive tax is imposed on the basis of an estimated taxable income. Presumptive income is exogenously determined. The base for the presumptive income tax is fixed and does not depend on the behaviour of individual entrepreneurs. In essence, a presumptive income tax works like a lump sum tax and therefore does not impose marginal tax burden on actual income. Varying methods of presumptive taxation are in operation in Israel, Argentina, Chile, and Columbia. The French *forfait* system is a typical example of presumptive taxation. The chief advantage of presumptive taxation is its simplicity, both for the tax collectors and the taxpayers. It is, therefore, cost-effective for the administration. The simplicity attribute may also encourage tax compliance. Presumptive taxation particularly suits the developing countries with a large unorganised business sector consisting of small retail establishments, and self-employed professionals. It is easy to administer this tax which can become an effective source of revenue. It also promotes horizontal equity. The French forfait system has several features. Firstly, the taxable profit of a given business unit is agreed upon mutually between the tax authorities and the assessee. Secondly, the assessment remains valid for a limited number of years. Finally, the taxpayer is required to submit a set of simple facts to the authorities, namely the amount of his purchases and sales, the wage bill, the value of his inventory, and the number of employees. Alternatively, small businesses may be subject to a system of licence fee charged in accordance with some well-defined criteria such as the location of business and its size.

13. Financial Action Task Force (FATF) is an inter-governmental body established in 1989 by the Ministers of its Member jurisdictions. The objectives of the FATF are to set standards and promote effective implementation of legal, regulatory and operational measures for combating money laundering, terrorist financing and other related threats to the integrity of the international financial system. The FATF is therefore a *policy-making body* which works to generate the necessary political will to bring about national legislative and regulatory reforms in these areas.

    The FATF has developed a series of Recommendations that are recognised as the international standard for combating of money laundering and the financing of terrorism and proliferation of weapons of mass destruction. They form the basis for a co-ordinated response to these threats to the integrity of the financial system and help ensure a level playing field. First issued in 1990, the FATF Recommendations were revised in 1996, 2001, 2003 and most recently in 2012 to ensure that they remain up to date and relevant, and they are intended to be of universal application.

    The FATF monitors the progress of its members in implementing necessary measures, reviews money laundering and terrorist financing techniques and counter-measures, and promotes the adoption and implementation of appropriate measures globally. In collaboration with other international stakeholders, the FATF works to identify national-level vulnerabilities with the aim of protecting the international financial system from misuse.

    The FATF's decision making body, the FATF Plenary, meets three times per year.

14. Asia/Pacific Group on Money Laundering (APG) is an international organisation (regionally focused) consisting of 41 members and a number of international and regional observers including the United Nations, IMF, FATF, Asian Development Bank, ASEAN Secretariat, Pacific Islands Forum Secretariat and World Bank.

    APG is closely affiliated with the Financial Action Task Force (FATF), whose Secretariat is located in the OECD headquarters in Paris.

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