

CHAPTER 19

IMPACT OF BLACK MONEY ON THE INDIAN ECONOMY AND WAYS TO BRING IT BACK FROM TAX HAVENS

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ABSTRACT

The generation of Black Money is problematic for developing nations as well as developed ones. It not only creates difficulties for honest taxpayers, but also destabilizes the a nation's economy. Black money can be defined as untaxed income that is evaded by evaders to gain personal gains and financial loss to the government of the nation. A nation's government can ratify a perusal of International Conventions and Treaties that can play an important role in bringing unessential illegal money back from the tax havens. The author has tried to bring forward the reasons of creation of black money in a country like India and the ways in which its circulation can be stopped. The Research Question focuses on the sufficiency of laws to combat this menace and is a connecting link between 'what is being done' and 'what has to be done' in present circumstances of Indian Taxation system including a look at the functioning of various bodies of the government and their role in maintaining transparent flow of money in the Indian economy. The Research Methodology adopted is Doctrinal in nature including the principles of applied research and Literature Review focuses on articles and books written by eminent authors expert in the field of economics and taxation.

Keywords: Black Money, Developing, Economy, Tax havens, Doctrinal.

1. INTRODUCTION

Black money is so much a part of our white economy, a tumor in the center of the brain- try to remove it and you kill the patient.

- Rohinton Mistry

India got independence in 1947 and framed its Constitution in 1950. The founding fathers of the Indian Constitution were vigilant enough to include the principles of equality, liberty and fraternity in the text. They gave the power to the citizens indirectly, by making them eligible to elect their representatives through the process of election. Their zeal to make India a powerful nation having roots of transparency, honesty and perseverance prompted them to include provisions of taxing system through Article 265 of the Indian Constitution. They wanted India to have the best infrastructure, less dependency on foreign nations, and a robust mechanism for development and all this was possible by creating a transparent and efficient taxing

system where people will pay tax as per their income and thus help in the overall development of the nation. There have been many statutory laws made by the Parliament of India from time to time, the most important one being Income Tax Act of 1961 and CGST Act of 2017 which describe the mode of taxation and the limits thereon. There are many other laws and authorities related to tax and its collection in India like Black Money (Undisclosed Foreign Income and Assets) and Imposition of Tax Act, 2015, Wealth Tax Act, 1957, Expenditure Tax Act, 1987, Central Board of Direct Taxes, Central Board of Excise and Customs etc. There have been many highlighting cases where people have been accused of stealing and evading the money that was supposed to be given to the government in form of tax. The question that arises here is how have they been able to do this? Is it the loopholes in the taxing system or the tricky mind of people, or something else? For answering this question, let's try to understand the basics of taxing system in India by figuring out the difference between tax avoidance and tax evasion. Tax Avoidance, is taking benefit of the loopholes present in the taxing system of a nation and is usually done by a person to lower down or minimize the tax. It is not illegal and includes legal activities in accordance with tax rules and regulations. Tax evasion, on the other hand, is illegal as it involves the difference between the amount of income that should have been legally reported to the tax authorities and the real income so reported and it is possible when the concerned taxpayer fails to give the amount in form of tax that was supposed to be given by him. There are many people in India who do not report the authentic source of their income to the Tax authorities and succeed in escaping the liabilities. The money collected in form of taxes is used by the government for making roads, highways, and expressways, laying down railway tracks, opening schools, colleges, hospitals, etc. Infrastructural development takes a severe hit when the money that was supposed to be utilized for development projects, is stashed in tax havens like Swiss Banks, etc. In a developing country like India, it is very important to make best use of the present infrastructure and ensure proper implementation of schemes related to economy of the nation. Therefore, it is equally important to have a transparent, strict and rigid model of taxing system laying down responsibilities of the taxpayers in a clear and defined manner so that they cannot hide any money or the source of money from the income tax authorities. As per the report published by the Standing Committee on Finance of the Government of India, the government of India has taken various steps like signing Tax Treaty framework with 146 nations, joining the Multilateral Competent Authority Agreement for automatic exchange of information, Double Taxation Avoidance Agreement etc. As per the report published in Down to Earth magazine, the International Monetary Fund estimates the global revenue loss to government due to the failure to give whole requisite amount as tax, at between \$200 billion and \$600 billion. This is a loss to both developed and developing countries. However, the developed nation can stand even after facing the cases of tax evasion up to some extent, but the country which is still developing suffers a lot as the money stashed in tax havens could have been used for the welfare of citizens and developing internal infrastructure.

2. REASONS OF BLACK MONEY GENERATION

There are many reasons of the generation of black money in an economy and most of them are related to visible loopholes in the taxing system and the lust of a person to earn more and more for living a better

standard of life. However, it doesn't mean that these are the only reasons for this problem as ill-conceived policies; corruption, high taxes, etc. are also there.

2.1 Weak political will and fragile policies of government

In order to stop the efflux of money from a nation to the tax havens, it is necessary to have a strong, transparent and potent taxing system and political will on part of the government to take action against the people who have been accused of stashing their untaxed money in foreign banks like the Swiss bank and when a nation lacks all these things or any of them, it becomes easier for a person to go ahead with his *malafide* intention of hiding the source of income and thereby sending it to other nations. In addition to this, the lacklustre approach of a nation's government in nabbing the persons accused of tax theft plays a big role in creating a perception in the mind of the accused that the people sitting in the government are not going to take any stringent action against him and he should proceed further with his volition. Needless to emphasize the fact that these are not good signs for any developing nation.

2.2 Corruption and its den

Corruption on any scale is dangerous not only for a society but the nation at large. It has been seen that many government officials are hand in glove with the accused person and help him in sending his untaxed income out of India. The person planning to stash his money in foreign banks normally promises to give some share to the officials who find no reason for denying help to him. This den of corruption starting from the government officials makes it easy for the accused to proceed further and ultimately causes big loss to the government's exchequer and the economy of a nation. Nations like New Zealand, Denmark, Finland, Norway, Luxembourg, etc. have almost zero tolerance policy on corruption, therefore there have been almost nil cases of tax evasion reported from these countries and the report of Corruption Perceptions Index published annually by Transparency International reflects this. Developing Countries like India need to take example from these nations and start building up a foundation paving out ways for stopping internal corruption. This may include asking the government officials from time to time, mention their authentic and transparent source of income accompanied by an affidavit and the cross checking of all those documents strictly by the government and its reliable officials.

2.3 Base Erosion and Profit Shifting

As said earlier, Tax Avoidance is making use of the loopholes of taxing system of a nation. Sometimes, many establishments pay less tax by taking benefit of the exemptions that have been given in the taxing laws of a nation. The companies doing their business in different parts of the world or in different nations generally shift their turnover or the annual profits to those nations where they have to pay fewer amounts in form of tax due to less rates of tax. Ultimately, what it does is the loss of income or revenue to the nations that were charging higher taxes. This is Base Erosion and Profit Shifting. Base Erosion, as the name suggests, erosion of the tax of a nation that was charging higher taxes and was legally entitled to do so.

2.3.1 Double Taxation Avoidance Agreement

The government of a nation enters in taxing agreements with other nations to enforce and regulate the system of taxing. Section 90 of the Indian Income Tax Act, 1961 empowers the Central Government to enter into an agreement with the government of any country outside India for granting relief in respect of Income which has been doubly taxed or in respect of income tax chargeable to promote mutual economic relations, for avoidance of double taxation or evasion or avoidance of tax. Double Taxation Avoidance Agreement (DTAA) is one of the purposes for which a government may enter in an agreement with the other nation. It is a tax treaty signed between two or more countries having the objective of avoiding tax payers to pay the tax on same income twice. For e.g. a person who is a resident of India has gone to the United States for earning purposes. He is doing some work for which he is being offered remuneration by the company on which the US will charge income tax. The question that arises here is that what would be the scenario if India also decides to charge income tax from the person on the same income as he is a resident of India? To save him from paying the tax, twice on the same income in two different countries, India and US enter in an agreement called as the DTAA according to which, the person will not be asked to pay tax in India on the income that has been earned by him in United States as he has already paid tax on that income there or he will be given rebates while paying tax in that income in India. The objective of DTAA is to make it easy for a country to attract investments by providing relief on dual taxation but sometimes, people misuse it for their personal benefits. Round Tripping and Treaty Shopping are the methods which people adopt for this. In Round Tripping, the role of shell companies is there. Shell Companies are the companies that exist only on papers and have no active business dealings. They are illegal in India and are mostly made for the purpose of evading taxes. There may be bank accounts attached to these companies. So, when a person in India sends his money to a DTAA partner country for setting up a shell company and reinvests the same back in India in form of Foreign Direct Investment (FDI), the profit out of such investment cannot be taxed in India as there is a treaty between India and the other country. This ultimately causes loss to the revenue of the Government of India. On the other hand, the accused person involved in the process succeeds in evading the tax that was supposed to be given by him to the Government of India. Treaty shopping is when a foreign company comes to do business in a country for e.g. India and invests in the nation through a tax haven country.

2.4 Money Laundering

It is a process through which black money is converted into white money. Through this process, people separate the untaxed income or the money earned by them through illegal means from the source, and mix them with the white money and finally invest it. This is an indirect method of accumulating money for personal use by cheating the government. By taking advantage of the taxing loopholes, and taking corrupt officials with them, the accused person succeeds in taking away the money that was supposed to be paid by him in form of taxes.

3. IMPACT ON ECONOMY

The generation of black money in a nation is very much problematic for its economy. It not only disturbs the taxing system of the nation, but also hinders the overall growth of the economy. Due to the stashing of black

money in foreign banks, the government's exchequer takes a severe hit as the money that should have been deposited in it, is sent outside. More importantly, the agendas and planning of the government is also disturbed.

3.1 Failure of the implementation of government policies

In every nation, the government brings effective policies for ensuring welfare of the citizens. Needless to emphasize the fact that for the implementation of these policies, the Central government as well as the State governments in India needs funds and these funds will be obtained in form of taxes. But, due to the rise in black money, the steps taken by the government for helping the citizens fail at every level. The economy faces shortage of resources as much of the money that should have been utilized in the upliftment of the citizens and economy, is stashed away far in tax havens. The level of output in the economy is directly affected by tax evasion. The money sent to tax havens cannot or output in the home country. A nation's policy becomes open to the dictates of international capital if huge amount of money is sent out to tax havens. All these things ultimately lead to the slower development of the nation and its economy. As per an article published in THE HINDU newspaper, India could have been an \$8 – trillion economy, the second largest in the world and its Per Capita Income could have been seven times larger, if it did not have the black money.

3.2 Inflation

Increase in the prices of essential commodities and services can be covered in drawbacks of black money. The costs are higher which raise the rate of inflation. Due to limited resources, people start compromising and one of the examples is a child taking tuition due to poor and ineffective teaching in school ultimately increasing the cost of the family. The Central Bank of a nation, Reserve Bank of India in India's case, fails to control the supply of money in the economy which gives birth to inflation. The influx of unaccounted black money creates a rift between rich and the poor due to inflation.

3.3 Parallel Economy

Parallel economy means functioning of an unsanctioned sector in the economy whose objectives run parallel and in contradiction with the objectives of official or sanctioned or legitimate sector in the same economy. The effect of generation of black money is so large that it sometimes creates parallel economy in the country. The use of black money in doing illegal activities like this, giving rise to parallel economy, degrades the value of the currency been used in the nation. The economy of the nation takes a severe hit which results in unemployment, price rise, hoarding, etc. The influx of money through parallel economy creates disturbance in the transparent system of tax collection and forces the government to take steps for the citizens that may not be suitable for them like increasing arbitrary tax rates, etc.

3.4 Affecting the credibility of a nation

It won't be wrong to say that the generation of black money in a nation and its stashing in tax havens affects its reputation in the world. Other countries are reluctant to engage themselves in business with a nation where economy is not growing as per the standards. International bodies like International Monetary Fund (IMF) and World Bank are hesitant in giving loans to these nations. Economy is the backbone of every nation and that is why it becomes essential for it to keep a check on the taxing system and citizens' activities internally so that the image of the country is not tarnished at the global level because in an era of globalization, almost all the countries are interdependent on each other for their needs and the generation of black money will play spoiler in their mutual relations.

3.5 Increase in government's deficit

The money in form of tax that was supposed to be given to the government legally, when sent in to the tax havens, deducts the share of the government and ultimately pressurizes it to come up with strict and sometimes, costly policies for the citizens. For e.g. if 100 rupees were supposed to be given to the government in form of tax but the person has given only 40 rupees, this deficit of 60 rupees has to be balanced. In return, the government may increase taxes and borrowings and the latter leads to debt. In case of failure to balance the deficit, the government is left with no option but to decrease spending which ultimately affects the overall development.

4. A NEED TO BRING IT BACK OR STOP IT FROM GOING OUT

The government of India in the month of December, 2021 couldn't give any exact figure of the amount of money that is stashed in foreign banks. However, it said that more than Rs. 8644 crore has been brought to tax and penalty of more than 1294 crores has been levied on the defaulters. Even in absence of any exact figure it can be estimated that a huge sum of money belonging to Indians is stashed in tax havens, especially the Swiss bank, as the Swiss National Bank released its data telling that the funds held by Indians in Swiss banks has risen to Rs. 20,700 crore in the year 2020. Knowing the fact that India has already lost a lot of money that should have been deposited in the government's exchequer, it becomes important to stop the generation of black money in the nation's economy and chalking out ways to bring back the sum that has been illegally deposited in tax havens. The government of India has taken some crucial steps like making statutory laws for e.g. Black Money (Undisclosed Foreign Income and Assets) and Imposition of Tax Act, 2015, Fugitive Economic Offenders Act, 2018, The Central Goods and Services Tax Act, 2017, Prevention of Corruption Act, 1988, Prevention of Money Laundering Act, 2002, Lokpal and Lokayukta Act, 2013, etc. By using the provisions of the above mentioned laws, the Indian government, up to some extent, has succeeded in keeping a check on the influx and efflux of black money. However, some more important steps should be taken for better coordination between tax haven nations and India so that more transparency is ensured. Let us try to find out what all things can be done for this purpose.

4.1 Reforms in the taxing system

India has a well-advanced taxing system which allows the appropriate authorities to collect taxes from the citizens. However, if the government plans to reduce the tax rates up to some reasonable extent which is convenient for the taxpayer as well as the government, it will help in making people pay taxes transparently as they won't find it difficult or hard to submit their source of income. However, it doesn't mean that the government should relinquish its claims or be ready to get less money in form of taxes. A person earning more than Rs. 10 lakh per annum has to pay 30 percent tax which if wisely reduced to 25 percent can help everyone.

4.2 Digitalization of records and documents

In order to create a transparent record system, it is advised that the government should make a digital record for all kinds of dealings, contracts, agreements, etc. and ask the parties to do the transaction digitally and not in cash. It is difficult to maintain exact record of cash transactions and mostly black money is used in form of cash, especially in real estate sector. Digitalization helps in creating a clear picture of the transaction which helps in knowing about the source of earning money that has been spent or invested for a particular purpose and therefore more use of plastic money is recommended.

4.3 Strengthening the working of bodies dealing with black money

In India, the institutions dealing with black money are Central Board of Direct Taxes (CBDT), Enforcement Directorate (ED), Central Board of Excise and Customs (CBEC), Central Economic Intelligence Bureau (CEIB), Central Bureau of Investigation (CBI) etc. The working of these bodies is clearly defined. The Income Tax department is primarily responsible for keeping a check on black money as it is responsible for collecting tax in a fair manner. It, on the basis of information so received, looks into the matters of tax evasion and gives notice to the individuals who refrain from giving taxes in a proper manner or give only some amount of money in form of tax. It is important to devise methods to ensure that the officers of IT department don't play in the hands of corrupt people who have an intention to evade tax. For this, frequent scrutiny and surveillance should be ensured on part of the government and its officers.

4.4 Working with nations together to combat black money

India has played an important role in combating the menace of black money by aligning with different nations. It has asked the Swiss bank to share the details of tax defaulters or people having their black money stashed in the bank. The government of India should ask the Swiss bank to review its investment policy and the rules related to disclosure of details of a tax evader. India has Double Tax Avoidance Agreements with more than 80 nations today which is a welcoming step.

4.5 Right to Information

Funding to political parties in India should be brought under the scanner. The ambit of Right to Information should be increased and the details of donations given to the parties must be put on the website of Election

Commission in a transparent manner. The Income Tax department should be made capable and independent to inquire into the details of funding to political parties and their expenses in rallies, roadshows, etc. The grants or donations given to political parties should not be in form of cash and be made mandatory to be in digital form. This glassy approach will help in stopping the conversion of black money in to white.

CONCLUSION AND SUGGESTIONS

All of us shall stand on the same footing even after 74 years of getting independence thinking that India has not developed up to the extent its founding fathers have dreamt. Framers of the Indian Constitution had thought of taking the nation to new heights where every citizen will have his home and adequate means of livelihood. Their zeal to incorporate the principles of equality and freedom in the Constitution paved the way for citizens to develop themselves in the field of education, health, etc. But some of the selfish people have shattered their dreams by taking some harmful steps that should not have been taken. There are many nations in the world who have stringent laws for their citizens who are accused of corruption or evading taxes. Some important steps that can be taken to stop the generation of black money can be listed below.

- 1) In India, the organizational structure of tax authorities is well developed, but lacks in proper implementation of laws that regulate income tax. It is easy to bribe an individual who acts as per the whims and fancies of the person so bribing. This lust for money or undue desire to get more should be finished.
- 2) Proper implementation of government schemes and statutory laws should be ensured for dealing with the defaulters effectively. Harsh and strict punishment should be given to every person who is accused of tax evasion and it should be set as an example for others.
- 3) Tax haven nations have already agreed to share the names of the tax defaulters with India once the proof is given by India. It becomes the duty of the Income Tax department of the Indian Government to find out the names of these tax evaders with authentic proof and submit the details to the nation where their black money is stashed.
- 4) India should take the Action 13 Country by Country reporting of the OECD seriously and try to find out the ways to stop the generation of black money.
- 5) It is beneficial for India if the nation's government by keeping in mind the adequate resources it has, compares the condition of the nation with any other developed nation. It will help in taking all those steps that are supposed to be taken for taking the country forward with defined agendas. For e.g. sending a team to study the economies of least corrupt nations and who are developed as well like Denmark, New Zealand, Singapore, Finland, etc. can help in chalking out the ways helping the Indian government to formulate steps and policies for stopping the generation of black money.
- 6) The technicalities of taxing system should be made to understand to the citizens and if needed, should be modified in a manner which is beneficial for the nation at large. Multiple audit trails on income across the production chain should be ensured.

India would have been in the list of developed nations today, if this money that is stashed in foreign banks was utilized for the welfare of citizens by constructing more highways, roads, dams, airports, creating

services within India, laying down railway tracks, making defense schemes and weapons including aircrafts, etc. within the territory of India. Even today, there are many people in India who are forced to live below poverty line and the rich has become richer, and poor has become poorer. This division is only because of the financial status and that is due to the cupidity of some people who have snatched the rights of all the citizens by taking their money to other nations. It is high time when India should stand tall and take action against individuals or citizens who have deposited their illegal income in foreign banks and come out with potent policies related to agreements with foreign nations for giving the details of tax defaulters or tax evaders in a proper manner. The sooner it is done, the better it is.

We should not forget the words of John Adams-

Our obligations to our country never cease but with our lives.

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