



# **Measures to Tackle Black Money in India and Abroad**

## **Report of the Committee**

**Headed by  
Chairman, CBDT**

**Parts - I & II**

**2012**

**Government of India  
Ministry of Finance**

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# Part-I

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## I. INTRODUCTION

Twin issues of corruption and black money have attracted unprecedented public attention in the past few months in India. Political debates in Parliament and outside, media news and campaigns, public demonstrations, *dhamas* and fasts, Hon'ble Supreme Court's attention and observations, and the general public discourse, has been focused on these issues for more than past two years now. A host of cases relating to corruption have surfaced, such as 2-G spectrum allocation, CWG, Medical Council of India, illegal mining in Jharkhand, Karnataka, Odisha, etc. While in many of these cases, action was taken *suo motu* by the law enforcement agencies, in some cases action came after Hon'ble Supreme Court intervened in Public Interest Litigations (PILs) filed before it. A number of cases relating to money kept abroad also surfaced, such as Hassan Ali Khan and associates, accounts in LGT Bank of Liechtenstein (information received from German tax authorities), and recently accounts in HSBC Bank (information received from the Government of France) which are still under investigation.

1.2 Keeping these developments in view, government has taken various steps. The government announced<sup>1</sup> its five-pronged strategy formulated to deal with the problem of black money kept abroad. A study was commissioned<sup>2</sup> by the government, after a gap of 25 years, to estimate the quantum of black money inside and outside the country. The study is being conducted by three top national-level institutions viz. National Institute of Public Finance and Policy (NIPFP), National Institute of Financial Management (NIFM) and National Council of Applied Economic Research (NCAER). Law enforcement agencies have investigated several high-profile corruption cases, putting an unprecedented number of persons charged of offences behind bars. The present Committee was constituted<sup>3</sup> to examine ways to strengthen laws to curb the generation of black money in India, its illegal transfer abroad and its recovery. A Directorate of Income Tax, Criminal Investigation, was notified<sup>4</sup> to deal with criminal matters having financial implications punishable as an offence under any direct tax law. Joint Drafting Committee was formed<sup>5</sup> by the Government, with representatives of agitating civil society members, to draft a Lok Pal Bill. The bill was introduced in Parliament, debated and put to vote in its Special Session<sup>6</sup>. India ratified<sup>7</sup> the United Nations Convention Against Corruption (UNCAC). Decision was taken to triple the manpower of the Directorate of Enforcement, responsible for implementing the anti-money laundering law. These responses demonstrate government's resolve to tackle the twin issues of corruption and black money.

1.3 This multi-agency committee under the Chairman, CBDT as originally constituted, consisted of the following:-

- i. Chairman, CBDT – Chairman;
- ii. Member (L&C), CBDT – Member;
- iii. Director, ED – Member;
- iv. Director General, DRI – Member;
- v. Director General, Currency – Member;
- vi. Joint Secretary (FT&TR), CBDT – Member;
- vii. Joint Secretary, Ministry of Law – Member;
- viii. Director, FIU-INDIA – Member; and
- ix. Commissioner (Inv), CBDT – Member Secretary.

<sup>1</sup> In press conference of Union Finance Minister on 25<sup>th</sup> January, 2011 at New Delhi

<sup>2</sup> Announced by Union Finance Minister in his Budget Speech on 28<sup>th</sup> February, 2011

<sup>3</sup> Ministry of Finance (CBDT) OM vide F.No.291/15/2011-IT (Inv.I) dated 27<sup>th</sup> May, 2011

<sup>4</sup> Notification S.O.1226(E) dated 30<sup>th</sup> May, 2011 [No.29/2011 vide F.No.286/179/2009-IT(Inv-II)]

<sup>5</sup> Notified on 9<sup>th</sup> April, 2011

<sup>6</sup> 27<sup>th</sup> to 29<sup>th</sup> December, 2011

<sup>7</sup> India became the 152<sup>nd</sup> country to ratify the UNCAC on 12<sup>th</sup> May, 2011

1.4 The Committee was mandated to examine the existing legal and administrative framework to deal with the menace of generation of black money through illegal means including, inter alia,

- a) Declaring wealth generated illegally as national asset;
- b) Enacting / amending laws to confiscate and recover such assets; and
- c) Providing for exemplary punishment against its perpetrators.

1.5 The Committee was required to consult all stakeholders and submit its report within a period of six months. However, in view of induction of Shri S S Rana, Member (Investigation), CBDT, as Co-Chair of the Committee, and in view of the responses awaited from trade & industry bodies and some departments, tenure of the Committee was extended up to 31<sup>st</sup> January 2012. Subsequently, Shri K. Madhavan Nair, Member (Inv.), CBDT was appointed as Co-chair, Dr Poonam Kishore Saxena was inducted into the Committee as Member (L&C), and the tenure of the Committee was further extended up to 31<sup>st</sup> March 2012.

1.6 The Committee held meetings on 9<sup>th</sup> June 2011, 27<sup>th</sup> July 2011, 23<sup>rd</sup> September 2011, 21<sup>st</sup> December 2011, and 21<sup>st</sup> & 26<sup>th</sup> March 2012 to consider various dimensions of the menace of black money, its generation from various sources and transfer abroad. In the **first meeting** held on 9<sup>th</sup> June 2011, it was decided that each organization represented in the Committee would examine the existing legal and administrative framework, relating to its respective sphere of functioning, to deal with the menace of generation of black money and prepare a status note including suggestions for improvement. It was also decided that a dedicated e-mail id would be created for inviting opinion from all stakeholders on declaring wealth generated illegally as national asset, enacting / amending laws to confiscate and recover such assets and providing for exemplary punishment against its perpetrators. After the first meeting on 9<sup>th</sup> June 2011, an exclusive email ID **bm-feedback@nic.in** was created to receive feedback from the public and uploaded, along with copy of the OM<sup>8</sup> constituting this Committee, on the web-site of the Income Tax department <http://incometaxindia.gov.in>, and a link provided therein for suggestions. Letters were addressed on 24<sup>th</sup> June 2011 to major trade & industry associations and other stakeholders for their response / suggestions in the matter by 15<sup>th</sup> July 2011.

1.7.1 In the **second meeting** of the Committee held on 27<sup>th</sup> July 2011 the Chairman informed that over 3,500 email responses had been received in the past four weeks. He listed out some of the main suggestions received:

- a) Electoral reforms, including state funding of elections.
- b) Tightening of laws, increasing the severity of punishments, and trial of cases relating to illicit money generated and stashed abroad through fast track courts.
- c) Confiscation of undeclared assets or money kept abroad.
- d) Monitoring of persons travelling frequently to tax havens and persons indulging in frequent transactions overseas.

1.7.2 The Chair further informed that responses to letters written to trade and industry associations, and others, were still to be received. The DG, DRI and Special Director, ED emphasized the criticality of information sharing among various law enforcement agencies for successful enforcement of the law. The Director, FIU-IND, informed that, under the Financial Intelligence Network (FINnet) being implemented, access to FIU-IND databases would be provided to enforcement agencies through nodes established in their offices. This would enable the member agencies to have speedy and efficient access to the information available with FIU. He also stressed the importance of regular feedback on information disseminated by FIU to improve the quality of suspicious transaction reports and the analysis function of FIU. The DG, Currency pointed out that security of currency is critical to combat the growing menace of counterfeit

<sup>8</sup> Ministry of Finance (CBDT) OM vide F.No.291/15/2011-IT (Inv.I) dated 27<sup>th</sup> May, 2011

currency. However, he raised the issue of huge economic cost of de-monetizing higher denomination bank notes of ₹ 500 and ₹ 1000 and stated that it was not a feasible idea. The JS (FT&TR), CBDT informed that while the issue of treating tax evasion a criminal offence was still being internationally debated, the flow of information has improved but the information received can be used only for tax purposes. He also informed that further progress had been made in the arena of international cooperation in tax enforcement by way of incorporating provisions in the Tax Information Exchange Agreements (TIEA), whereby enquiries can be made through Indian missions abroad in the presence of officials of that country and counsels of persons investigated. After the second meeting, reminder letters were again sent to the trade / industry associations on 18<sup>th</sup> August 2011, requesting their inputs / suggestions by 15<sup>th</sup> September 2011.

1.8 The **third meeting** of the Committee, held on 27<sup>th</sup> September 2011, discussed at some length various suggestions of the participating organizations and the public. The Chairman observed that existing laws were enough to deal with economic offences but there was a need to strengthen the administrative mechanism to enforce the existing laws. It was observed that existing information exchange mechanism should be improved and additional manpower and financial resources provided to the investigating agencies to tackle the scourge of black money. The Committee noted the anomaly in the existing provisions of the Income Tax Act, 1961 in respect of re-opening of assessments in cases where black money stashed abroad pertained to beyond six years and agreed that an amendment in the Income Tax Act was warranted to rectify this situation. It was also agreed that there was urgent need to better regulate the real estate sector, considered as one of the largest contributors to black money. The Committee was informed that proposals for strengthening PML Act 2002 have already been submitted to the Department of Revenue and were under active consideration of the government. The DG, Currency informed the Committee that maintaining the security of currency is of critical importance and therefore the currency rules have been recently amended to upgrade the existing security features.

1.9 The **fourth meeting** of the Committee, held on 21<sup>st</sup> December 2011, discussed the basic structure of the Report, viz. define and differentiate 'black money' and 'dirty money' and the sources of its generation. The Chairman emphasized the importance of laying to rest common misconceptions as regards black money through a comprehensive report. He pointed out that black money is first generated within India and then some of it is transferred abroad, and that one of the most important sources of black money within the country is leakages from public expenditure. The Co-Chair informed that feelers were coming from the business community, particularly from the gems & jewellery sector, that the black money holders may be allowed to come forward with disclosure of unaccounted income and assets both in India and abroad, but without any harassment or threat of prosecution and for that purpose the Government should bring out a disclosure scheme exempting prosecution under the Income Tax Act. The Committee noted the views expressed by JS (FT&TR), CBDT that although tax treaties are subject to domestic laws, some countries such as Belgium, Sweden, Norway, etc., allow repatriation of black money, and in this light there is a need to create international consensus regarding recovery of black money, which is otherwise possible only under United Nations Convention Against Corruption (UNCAC) and Mutual Legal Assistance Treaties (MLAT), or through specific recovery provisions in tax treaties. There is no international consensus or law anywhere for declaring tax evasion a criminal offence, but there is a need to distinguish tax evasion from legal and illegal sources. The Committee also noted the issue raised by Member (L&C), CBDT that one of the main contributors to black money in the country is out-dated laws and their lax administration by the state governments, such as stamp duty values being completely out of line with the prevailing market rates, and it was incumbent to suggest action by the state governments to tackle the menace of black money as important stakeholder in controlling it. The Committee further noted the facts pointed out by DG Currency that several steps have been taken to deal with the problem of leakages from the public expenditure, improve the public procurement system and allocation of natural resources following recommendations of the Dhalla and Chawla Committees<sup>9</sup>. The Committee also noted with concern the

<sup>9</sup> Constituted vide Order No.483/1/1/2011-Cab. Dated 31.01.2011

issue that although FICN forms only a small part of black money as pointed out by DG DRI, more effective measures were required to counter its debilitating consequences. On the suggestion of Director FIU-IND that on account of most of the black money going out of the country through banking channels, there is a need for a central repository of such data, the Committee agreed that the proposal was worth considering. After the fourth meeting, further reminders were sent to Member agencies and trade / industry bodies.

1.10 In response to the reminders, FICCI and ASSOCHAM replied, which are at **ANNEX-A1** and **ANNEX-A2**, respectively. Gist of suggestions from over 4,000 emails received from the public through [bm-feedback@nic.in](mailto:bm-feedback@nic.in) is at **ANNEX-A3**.

1.11 The Committee held its **fifth** meeting on 21<sup>st</sup> March, 2012. The Chairman suggested that for deterrent effect, with the aim of fast-tracking through summary trials, the maximum imprisonment of three years prescribed for some of the less serious economic offences may be considered to be reduced to two years by the respective departments. He also suggested that the maximum punishment for more serious offences under the PC Act may be considered to be enhanced from the prescribed seven years to ten years. The suggestions were endorsed by the Committee. It was suggested by the Co-Chair that there should be some limitation of carrying and holding of cash for personal use, for which either the existing laws may be amended or a new law enacted. This was endorsed by the Committee. The draft of the report was decided to be accordingly amended.

1.12 In the **sixth** and final meeting held on 26<sup>th</sup> March 2012, suggestion of Member (L&C), CBDT to consider mandating application of Accounting Standards AS-7 and AS-9 to real estate sector was agreed to by the Committee. The suggestion of representative of ED that MCA should consider placing a cap on the number of companies operating from the same premises and number of companies in which a person can become director, and also that there should be better regulation of financial instruments such as PNs, was endorsed by the Committee. The suggestion of Co-Chair to ensure data security was also endorsed. It was also agreed that the Report would be amended accordingly before signing by the Members on 28<sup>th</sup> March, 2012.

1.13 The Chapters in this report have been arranged to examine (i) the existing popular, academic and international concepts and definitions of black money, to arrive at an agreeable view for the purposes of this report; (ii) the causes for generation of black money, and the sectors of the economy most prone to and / or affected by it; (iii) the extent of black money in India and abroad; (iv) the existing legal provisions and the administrative machinery to tackle black money; and (v) measures to tackle black money.

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## II. CONCEPTS AND DEFINITIONS OF BLACK MONEY

2.1 There is no uniform or accepted definition of 'black' money. Several terms are in use – such as 'black money', 'black income', 'dirty money', 'black wealth', 'underground wealth', 'black economy', 'parallel economy', 'shadow economy', 'underground' or 'unofficial' economy. If money breaks laws in its origin, movement or use, and is not reported for tax purposes, then it would fall within the meaning of black money. The broader meaning would encompass and include money derived from corruption and other illegal ways – to include drug trafficking, counterfeiting currency, smuggling, arms trafficking, etc. It would also include all market based legal production of goods and services that are concealed from public authorities for the following reasons –

- (i) to evade payment of taxes (income tax, excise duty, sales tax, stamp duty, etc);
- (ii) to evade payment of other statutory contributions;
- (iii) to evade minimum wages, working hours and safety standards, etc.; and
- (iv) to evade complying with laws and administrative procedures.

2.2 There are three sources of black money – crime, corruption and business. The 'criminal' component of black money would normally include proceeds from a range of activities including racketeering, trafficking in counterfeit and contraband goods, forgery, securities fraud, embezzlement, sexual exploitation and prostitution, drug money, bank frauds and illegal trade in arms. The 'corrupt' component of such money would stem from bribery and theft by those holding public office – such as by grant of business, bribes to alter land use or to regularize unauthorized construction, leakages from government social spending programmes, speed money to circumvent or fast-track procedures, black marketing of price controlled services, etc.

2.3 The 'commercial' limb of black money usually results from tax evasion by attempting to hide transactions and any audit trail relating thereto, leading to evasion of one or more taxes. The main reason for such black economy is underreporting revenues / receipts / production, inflating expenses, not correctly reporting workers employed to avoid statutory obligations for their welfare. Opening of the economy permits contracts of all kinds – particularly for allocation of scarce resources such as mineral and spectrum – which, in the absence of transparent rules and procedures for licenses and non compliance of contractual obligations of the persons concerned, leads to increased generation of black money. In all the three forms of black money – 'criminal', 'corrupt' and 'commercial' – subterfuges are created which include false documentation, sham transactions, benami entities, mispricing and collusion. This is often done by layering transactions to hide their origin.

2.4 Studies correlating the extent of corruption with the size of the 'shadow economy' have been few. There is, however, reason to believe that it differs among high and low income countries. In high income countries, the official sector provides good governance and proper enforcement of contracts. In the developing countries, on the other hand, enterprises could engage in entirely unreported activity – restaurants, bars, doctors, lawyers – and even bigger manufacturing entities may indulge in under-reporting. Big companies, though easier to monitor – in order to escape rigours of taxation – may take recourse to inducements. Under such socio-economic conditions, the 'underground' economy and corruption are likely to reinforce each other.

2.5 Level of development affects extent of black economy in another way. Developing countries have large parts of their economy in the informal sector, which is difficult to regulate. Further, cash component of the economy is usually higher and leads to problems of monitoring. Lack of regulation and monitoring reinforces the black economy and also helps its expansion. Opportunities for leakages increase. Low level of literacy reduces penetration of the banking sector resulting in a large cash economy.

2.6 For the purposes of this report, we shall interchangeably use two terms – ‘black money’ to broadly mean unaccounted or undisclosed income and assets not reported for tax purposes, without reference to its origin (whether legal or illegal), and ‘black economy’ to denote the sum total of incomes / assets as well as activities that are not accounted for.

2.7 Inflation of expenses takes money out of the system and, therefore, turns ‘black’. Wrong claims of deductions or incentives provided in the law reduce the tax liability and thereby keep more funds with the concerned person than with the State. However, money in this case remains within the system and cannot be said to be unaccounted or ‘black’. Similarly, shifting of profit for taxation outside the country through transfer pricing by related concerns results in organizing a reverse capital flow from poor to rich countries. This also cannot be said to be ‘black’ in that money does not go ‘underground’. However, these aspects are also discussed in the report as they reduce substantially the availability of resources for economic development of the country.

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### III. CAUSES & METHODS ADOPTED FOR GENERATION OF BLACK MONEY, MOST PRONE SECTORS OF ECONOMY<sup>10</sup>

3.1 Generally, rising burden of taxation, both actual and perceived, provides a strong temptation to participate in the black economy. Increasing burden of compliance also gives a strong reason to enter the black economy. Lack of tax morality, or non-compliant attitude of the citizenry towards tax laws, also tends to increase the size of the black economy. Studies indicate that countries with relatively poor regulation of their economies tend to have a higher share of unofficial economy in the GDP, while countries with proper regulations have smaller 'black' economies. Developing countries generally have higher levels of controls, leading to significantly higher effective taxes on official activities, a large discretionary framework of regulations and, consequently, a higher 'black' economy. Developed countries tend to have better enforcement of laws, balanced regulatory burden, better tax to GDP ratio resulting in sizeable revenue mobilization and, therefore, relatively smaller 'black' economies.

3.2 While in developed countries / areas like USA, Canada and Europe black money is generated primarily through illegal activities such as drug trade, illegal migration, etc., in the developing countries in Asia and Africa, generation of black money is from all conceivable sources – corruption and siphoning of public resources, trade-based black money due to non-reporting of incomes or profits and inflation of expenses, and through a host of criminal activities such as illicit manufacturing of counterfeit goods, smuggling, extortion, cheating and financial frauds, illicit narcotics trade, printing and circulation of fake currency, illicit manufacturing / trade in arms, ammunition and explosives, etc.

3.3 Thus, the fight against generation and accumulation of black money is likely to be far more complex requiring stronger intervention of the state in developing countries like India, than in the developed countries. This needs stronger legal framework and commensurate administrative measures, and still stronger resolve to fight the menace.

#### **Suppression of receipts, inflation of expenditure, etc.**

3.4 The primary method of generation of black money remains suppression of receipts and inflation of expenditure. The suppression could be over a range of businesses and industrial activities which are covered by what may be called 'primary' enactments to regulate sale receipts, actual production, charging amount in excess of statutory amounts, etc. Duties are imposed on manufactured goods through the Central Excise Act by the Central Government. However, the states of the Indian Union have a wide array of powers under List-II of the Constitution. If we take by way of example – two states, namely Uttar Pradesh (U.P.) because of its large population and Madhya Pradesh (M.P.) because of its area, the Government controls economic activity by way of levying taxes, and secondly, by way of controlling certain industrial and commercial activities. U.P. has the Sales Tax Act of 1948 and M.P. has Commercial Tax Act of 1994. U.P. has an Entertainment and Betting Tax Act and Luxury Tax on hotels. Both states have Excise Act by which taxes are levied on liquor manufacture, Stamp Act to deal with collection of stamp duty from registration of instruments for transfer of immovable properties. The primary and fundamental reason for suppression of receipts or values is to lower the incidence of tax. These states also have laws to regulate certain trades – U.P. has Regulation of Cold Storage Act, Regulation of Money Lending Act, Sugar Cane (Regulation) Act and Supply and Purchase Tax Act. The Madhya Pradesh Tendu Patla Adhiniyam, 1964 regulates the trade of Tendu leaves by creation of state monopoly in the trade.

3.5 Therefore, the Income Tax Act becomes a 'secondary' Act. What is hidden from state authorities cannot be shown for the purpose of income tax, as such hidden element is already a part of the 'black' economy. Moreover, if an income tax investigation subsequently reveals infringement of state laws, the courts tend to favour the transgressor, as the evidence of his records have been 'accepted' by state authorities.

<sup>10</sup> Inputs mainly from the Income Tax Department

3.6 However, as manipulation of income is not always possible by suppression of receipts, tax-payers may try to inflate expenses by obtaining bogus or inflated invoices from 'bill masters', who make bogus vouchers and charge nominal commission. As these persons are of very modest means, upon investigation, they tend to leave the business and migrate from the city where they operate. This is one of the reasons for a proportion of income tax arrears attributed to 'assessee not traceable'.

3.7 Similarly, there are other categories of small 'entry operators', who provide accommodation entries by accepting cash in lieu of cheque/ demand draft given as loans / advances / share capital, etc and thereby launder large sums of money at miniscule commissions. Due to frequent migration, such entry operators escape prosecution under the Income Tax Act. The appellate tax bodies also tend to tax their income at nominal rates. There is no effective deterrence, except for taxing commission on such bogus receipts and tax in the hands of beneficiaries. Providing fake bills and entries need to be dealt with strongly and as criminal offence under the tax laws.

### **Land and real estate transactions**

3.8 Land and real estate are possibly the most important class of assets used for investment of 'black' money. As immovable properties are not usually comparable, valuations are different. This imparts flexibility to the valuation process, and makes it an ideal investment for 'black' money. As an asset class both 'black' and 'white' savings are utilized for investment in land and real estate, which provides hedge against inflation apart from a profitable alternative for investment for black savings.

3.9 The availability of urban centres and developed areas critically depends on the policy of the government as change of land use and development of infrastructure is largely in its hands. If resources are concentrated on developing infrastructure in select areas then development accentuates land and property prices in these areas. Master Plan of an urban agglomeration is many a time found to be changed and re-changed again. The more developed parts exert a pull on the less developed parts and infuse a push in prices. Such change is at a 'cost' to the developer paid from the black component of his business.

3.10 Fiscal statutes and incentives both impede and impart momentum to investments in real estate. As a result of rapid urbanization and rising pressure on land in the vicinity of urban areas, real estate prices have increased exponentially. Earlier, Chapter XX-C of the Income Tax Act, 1961 provided for pre-emptive purchase by the Central Government, in cases where agreed consideration of properties was less by 15% or more of the fair market value in designated areas. However, as these provisions were causing procedural delays in registration of transfers, and with a view to remove a source of hardship for the tax-payers, the provisions of Chapter XX-C were made inapplicable in respect of any transfer of immovable property on or after 1st July, 2002. The provisions of Section 50C were brought in by the Finance Act, 2002 w.e.f. 1.4.2003, providing for adoption of stamp duty rates for the purpose of computation of capital gain in the hands of the seller. As levy on land is a State subject, the revision of land rates varies from State to State. Mostly, the stamp duty rates or 'circle rates' are fixed in a general manner, on the basis of zoning of municipal areas — often into 'commercial', 'residential', and 'industrial', etc. These circle rates offer a criterion for differential valuation of different locations but may not reflect actual valuation of individual properties. The present arrangement is therefore not satisfactory and not as effective as Chapter XX-C in curbing both the generation and utilization of black money in the real estate sector.

3.11 With rapid urbanization, large areas of farmlands fall in the urban agglomeration of metros, emerging metros and large cities. Surveillance indicated that cash rich individuals or other entities generating black money through suppression of production profits of pan masala, oil, para-banking, big corporate houses, etc., paid large sums of purchase consideration in cash to farmers. Such acquisition of land by cash payment has the consequence of facilitating routing of black incomes and as farmers move elsewhere, chargeability of capital gains on sellers, i.e. farmers, cannot be effected. Section 194LA of the Income Tax Act, 1961 provides for tax deduction at 10% on the compensation against compulsory acquisition of immovable property. The provision was not made applicable to agricultural land even though such land was falling within 8 kms of a municipality or a cantonment board. Presently, the only way the Income Tax

department monitors such payments is through the Central Information Branch (CIB), where such information is obtained from the Registrar of properties. There is reluctance to comply with the requirement, and it also involves a time lag before the assessing officer is seized of the matter, and because of the time lag verification of on-money payments is not possible. The provision of tax clearance certificate under section 230A of the Income Tax Act was earlier withdrawn in 2001.

3.12 In the real estate sector, despite accounting guidelines<sup>11</sup> for recognizing revenue by percentage completion methods, real estate firms (mostly private companies), resort to their own subjective ways. Some companies show income when a project is say only 30% complete to avail of bank credit, and if there is ample liquidity, not to follow accounting principles by not showing income when a project may be 90% complete. Such accounting variations are larger in this sector of the economy than any other. This is because ICAI Accounting Standards (AS) No.7 (percentage completion method) prescribed for construction contracts leaves out real estate developers. AS No.9, which prescribes standard for revenue recognition, as well as AS-7 are not yet notified under the Income Tax Act. Besides, inflated purchases and wages are shown and project incomes adjusted to under-report profits to the Income Tax department. With labour and materials sourced from the unorganized sector, the scope of inflation of expenses is higher. The actual margin of profit – depending on the land bank holding – may vary substantially from 8% of contractors profits on land acquired just before development to as high as 60% where such land bank has been acquired earlier. The larger projects – civil infrastructure works, like roads, bridges sometimes follow ‘inventive accounting’ – where revenue items receipt is carried to the balance sheet after ‘adjustment’. Such civil works also have scope for manipulation, as the tender amount at a lower figure is side stepped by the successful bidder through cost escalations permitted by conniving staff of the Government agency concerned or through arbitration. Most of the contracts have ‘on-money’ and ‘illegal’ components, and their inter-lacing with disclosed component, makes monitoring of the real-estate sector and civil works extremely difficult.

3.13 With continuous rise in prices along with tax benefits on residential properties, high-net worth individuals are motivated to invest in properties, mainly with a view to transferring them and encashing the ‘gain’ as capital gain, which enjoys special tax treatment and benefits. As a result their investment would not generate desirable activity, as sales on investments of a residential house are tax-free, if re-invested. Such ‘flipping’ provisions of Section 54 usually help high net-worth individuals. From the angle of welfare of the community, the investment gets channelized to an unproductive activity – speculating in the price of real-estate. Often, the agreement to sell is not executed by the original buyer(s) but by the last buyer, where intermediaries charge hefty premiums.

## **Corruption**

3.14 The cancerous growth of corruption at every stage of interface of the public with officials by way of commissions on mega-projects, kick-backs on mega purchases abroad, leakages in public spending, are all a matter of serious concern.

3.15 In India, it is widely reported that corruption is pervasive and appears impossible to eliminate. At the grass root level, corruption is practiced in millions of exchanges that ordinary people have at lower levels of bureaucracy – for licenses, procuring services, etc. – as part of government’s delivery mechanism. Cumulatively a punitive cost is imposed on the poor and lower middle classes. In contrast, instances of large-scale corruption at the national and regional scale, though distant from petty instances of everyday life, have a shock and awe effect and tends to provide a rationalization for lower level corruption. In the Corruption Index for 2010 prepared by Transparency International, India ranked a lowly 87 out of 178 countries (Brazil, China are better placed). In the latest report of 2011, India’s rank slipped further to 95 out of 182 countries, whereas Brazil, South Africa and China continue to be ranked higher. Perception of administrative and political corruption in India has risen, with the country having fallen 8 places on

<sup>11</sup> Indian Accounting Standards (AS) 7, 9 and 11 issued by the Institute of Chartered Accountants of India

Transparency International's Corruption Perception Index. **TABLE-C1** indicates the position of BRICS nations (Brazil, Russia, India, China & South Africa) in the Corruption Perception Index in perceived levels of corruption rankings – a very high score indicating very clean systems and very low score indicating highly corrupt countries.

3.16 The 'Ease of Doing Business' index of the World Bank ranks countries on ten parameters, namely, starting a business; dealing with construction permits; getting electricity; registering property; getting credit; protecting investors; paying taxes; trading across borders; enforcing contracts; resolving insolvency. This index averages the country's percentile ranking on ten topics, giving equal weight to each topic – benchmarked to June, 2011. India is a lowly 132 (out of 183 countries) on the Ease of Doing Business Index as against high ranking developed countries like Singapore, UK and USA, or even BRICS nations, as depicted in **TABLE-C2**.

3.17 It is widely believed that the election process requires considerable funds whereas resources declared by major political parties do not appear to be sufficient to meet the actual expenditure and therefore are believed to be funded also through black money. Further electoral reforms are also required to reduce election costs. With increased economic activity, bribes in public private partnership of large projects and large civil works have been detected. Allocation of natural resources is allegedly discretionary and non-transparent. Corruption has also been alleged in defence procurement, foreign consultancy, aircraft purchases, petroleum and gas sectors, purchases abroad, etc. It is reported that despite prohibition on kickbacks in the developed world, ways are found to make such payments through spurious agreements and shady entities, which in turn are alleged to be secreted away in bank accounts in tax havens.

3.18 The thrust of reforms initiated in 1991 was to open the economy. However, free markets need regulatory institutions with best international practices of transparent processes – otherwise, it emasculates democracy. Social sector schemes involving huge public expenditure reportedly suffer from possible manipulations and leakages. Direct transfers to the accounts of beneficiaries can provide a solution, as it would prevent manipulations like bogus muster rolls. There is a need for effective implementation of KYC norms with adequate safeguards and controls in rural areas without adversely affecting promotion of financial inclusion of the rural population.

3.19 Co-operative banks perform the critical function of providing banking and financial services in rural and far-flung areas where normal banking services are not available. The banking operations of co-operative banks are regulated by the RBI Rural Planning Credit Department and RBI Urban Banks Department. There have been instances when co-operative banks have not been following KYC guidelines. On some occasions, co-operative banks have resisted giving information to the Income Tax Department.

3.20 Corruption of, and in, the private sector is an issue not much in public focus or debate. Corruption flows from private motive or greed, fuelled by discretionary powers vested in an office empowered to distribute resources, goods and services to public. Dishonesty in private sector, for private benefit or profit, is largely responsible for bribery, siphoning of public funds and leakages in public expenditure. It also results in conspicuous consumption, money laundering and sustenance of the black economy. The way to deal with private greed is to design well-laid down rules and regulations, and ensure their proper enforcement and transparency in decision-making without compromising trade interest.

### **Financial market transactions**

3.21 While some sections of the financial markets have become better regulated, many sections remain relatively unregulated. Advances in technology provide possibilities of better reporting systems.

3.22 Investments are made in the secondary share markets with a view to capturing gains. In this market, out of nearly 8,000 listed companies, several scrips are not traded regularly. With the collusion of promoters, some brokers arrange for price(s) with purchase of such scrips at nominal costs, and sales at exorbitant prices, with a view to receiving money on sale as 'capital gain' when the long term gain is subjected to a 'nil' or nominal rate of tax. The advantage for manipulative taxpayer is that he can launder such sale receipts through payment of no tax.

3.23 Often price sensitive information is obtained and the gain is sought to be made on the basis of asymmetrical information, involving 'insider-trading' and also 'fronting', through intermediary companies, which hide the individuals behind the corporate veil. Though SEBI is an effective regulator, instances of 'insider-trading' or 'fronting' are not unknown. Though the stock-exchanges have internal audit, intermediaries are permitted to make genuine corrections in the last fifteen minutes, in respect of transactions entered into by them. However, instances of collusive corrections being made by brokers for obliging clients, using the term 'fat finger' for collusive deals, usually losses have been reported both in the share and derivative segments of the stock market. 'Dabba-trading' or trading outside the recognized stock exchanges, similarly contribute to the parallel economy.

### **Bullion & jewellery transactions**

3.23 When controls were removed, smuggling of gold reduced and legal imports increased. As per the World Gold Council<sup>12</sup> in the twelve month period ended Q-3, 2011, the consumer demand for gold in India stood at 1059 tonnes, valued at US \$ 50 billion approx, as against 808.7 tonnes for Greater China, 213.5 for the USA and the world total of 3427.4 tonnes. According to WGC estimates<sup>13</sup>, India holds over 18,000 tonnes of above ground gold stocks, worth over US \$800 billion (nearly 2/3<sup>rd</sup> of India's current GDP) and represents 11% of gold stock. The easing of import duty has reduced the intent of illegality but owing to socio-cultural reasons of Indian society, the economic impact of gold remains. As most of the bullion and jewellery is imported, it puts pressure on the balance of payments position, and is also open to misuse by illicit transfers abroad, as gold imports are 11% up in terms of tonnage and 44% in terms of value from January to September, 2011. At \$37 billion, so far in the year, it has disproportionately increased the import bill in FY 2011-12 and also adversely impacted the balance of payment. Schemes for importing gold and re-export after value-addition are abused, when gold is diverted to meet domestic demand. Another possible reason is that deposits in banks – either in savings accounts or in fixed deposits or mutual funds do not guarantee a rate of return that would protect the value of investment and have thus made gold a natural choice for investment as it ensures appreciation as well as liquidity. For the country as a whole, high import payments contribute to making the current account deficit larger, creating inflationary pressures and making imports more expensive in rupee terms.

3.24 For the reason that gold has high intrinsic value, it is preferred as an asset class for hiding 'black' incomes even in times of high inflation or uncertainties plaguing the economy, and despite chargeability of jewellery, gold and bullion to wealth tax. The investment in gold is unproductive as, instead of imparting momentum to the economy, citizens in India hold on to such sterile investment for capital appreciation and financial security.

### **Cash economy and use of counterfeit currency**

3.25 'Cash' as an asset has its own demand. However, in large cash economies, such as India, counterfeit currency poses a major threat to the economy. Countries have attempted to check counterfeiting of currency notes, as it disrupts smooth commercial transactions and has a multiplier effect on mainstream economy. India faces this problem, as immigrants become carriers for small amounts. The Indo-Bangladesh, Indo-Pakistan and Indo-Nepal borders are targeted for this purpose by agencies inimical to the interests of India.

3.26 The demand for currency is determined by a number of factors such as income, price levels and opportunity cost of holding currency. Currency is also used as a store of value, particularly in countries with low inflation or large 'shadow' economies. As per the RBI Annual Report for 2010-11, there was acceleration in currency in circulation in 2010-11 owing to increased demand on account of economic growth, high inflation and low yield on deposits for most part of the year.

<sup>12</sup> Source: Thomson Reuters GFMS

<sup>13</sup> 'India: Heart of Gold Revival' – report of World Gold Council (WGC), 2010

3.27 **TABLE-C3** reflects the increase and uptrend in the currency to GDP ratio. It may be pertinent to add that value as well as volume of the bank notes continues to increase. In a comparison over three years, it may be seen from the table that the value of bank notes outpaced that of volume, reflecting the continuing shift towards high denomination notes, particularly those of Rs.1,000 and Rs.500 in value.

3.28 The use of currency is attributed to three reasons by the RBI in its Annual Report. Firstly, inflation remained high, often in double digits, in respect of commodities such as food grains, pulses, fruits and vegetables and milk during F. Yrs. 2009-10 and 2010-11 – where transactions are expected to be cash intensive. The share of agriculture and allied activities in nominal GDP increased from 17.6% in 2008-09 to 19% in 2010-11. Secondly, there was a step-up in real economic activity from 6.8% in 2008-09 to 12.5% in 2010-11. Thirdly the interest rate on bank deposits was generally lower than inflation during 2010-11, implying a negative real rate of return on deposits. The RBI in its latest annual report has attributed the growth and strength in the cash economy to factors like acceleration in per capita real GDP growth, commercialization of agriculture, urbanization and availability of higher denomination notes.

3.29 India has a large cash economy due to dependence on agriculture, and existence of non-formal sector and insufficient banking infrastructure. Further, the RBI has attributed the growth and strength in the cash economy to factors like acceleration in per capita real GDP growth, commercialization of agriculture and urbanization and availability of higher denomination notes. In a recent judgement delivered by Hon'ble Kerala High Court<sup>14</sup>, the Court has suggested putting restrictions on possession and handling of cash above certain limits. In an earlier case, Hon'ble Supreme Court had also observed<sup>15</sup> that *"The nation is facing terrorist threats. Transportation of large sums of money is associated with distribution of funds for terrorist activities, illegal pay offs, etc. There is also rampant circulation of unaccounted black money destroying the economy of the country."* Further, *"Money which is drawn from a Bank and legitimately belonging to the carrier, may still be used for an illegal purpose, - say to pay for a crime or to fund an act of terrorism. It may also be used for a routine illegal function - to make part payment of sale consideration for a property in cash, so that the full price is not reflected in the sale deed, resulting in evasion of stamp duty and registration charges and evasion of payment of capital gains and creation of black money. The carrying of such a huge sum, itself gives rise to a legitimate suspicion."* The Court concluded that, *"Any bona fide measures taken in public interest, and to provide public safety or to prevent circulation of black money, cannot be objected as interference with the personal liberty or freedom of a citizen."*

3.30 In recent years, the social sector expenditure by the Government particularly in rural areas in schemes like MGNREGS, etc., have also boosted demand for cash when the currency to GDP ratio peaked. The main difficulty with such transactions is that they have inadequate audit trail leading to leakages, estimated by developmental economists to vary between 15% and 40%. The oversight relies generally on financial audit. Increased currency use (**TABLE-C4**) in a fast growing economy is inevitable yet facilitates tax evasion, only underlying the increasing importance of proper adherence to KYC norms and reporting of large value transactions for tax purposes.

3.31 The Banking Cash Transaction Tax (BCTT) was in operation earlier to regulate large cash withdrawals. At the beginning of the Year 2012, the central banks across the world, including USA, Brazil, Australia, South Korea, Indonesia and Thailand, have pledged to bring down repo rates and release more liquidity into the system in the face of falling global growth expectations<sup>16</sup>. Such liquidity could flow into risky assets in the form of higher yielding currencies, like the Indian Rupee. Artificial liquidity is not desirable, as markets would be prone to using it for speculation and that would mean rising asset prices, with inflows in India likely to increase.

3.32 Demonetization of high denomination currency notes is believed to be one of the methods to 'kill' the extant black economy, and to curb the generation of black money. In India, demonetization was

<sup>14</sup> P.D. Abraham v. CIT (Central), Cochin Cross Objection 112/2008 in ITA 323/2008 dated 15.12.2008

<sup>15</sup> Rajendran Chingaravelu vs. UoI in CA No. 7914 of 2009; ORDER DATED November 24, 2009 (320 ITR 1)

<sup>16</sup> Media reports



implemented in 1946 and 1978. Experts have criticized that demonetization did not achieve the objective it was aimed at. Further, inflation over the years and a large cash economy requires higher denomination currency notes to keep the cost of monetary management of the economy low.

### **Trade Based Money Laundering<sup>17</sup>**

3.33 Financial Action Task Force (FATF) defines Trade Based Money Laundering (TBML) as the process of disguising the proceeds of crime and moving value through the use of trade transactions in an attempt to legitimize their illicit origins. In simpler terms, TBML is the process of transferring / moving money through trade transactions. In practice, this can be achieved through the misrepresentation of the price, quantity or quality of imports or exports.

3.34 The international trade system is subject to a wide range of risks and vulnerabilities, which provide unscrupulous entities the opportunity to launder money. The relative attractiveness of the international trade system is associated with:

- a) The enormous volume of trade flows, which obscures individual transactions and provides abundant opportunity to transfer value across borders;
- b) The complexity associated with (often multiple) foreign exchange transactions and recourse to diverse financing arrangements;
- c) The additional complexity that can arise from the practice of mingling illicit funds with the cash flows of legitimate businesses;
- d) The limited recourse to verification procedures or programmes in order to exchange customs data between countries; and
- e) The limited resources that most customs agencies have to detect illegal trade transactions.

3.35 Differing tax rates create incentives for corporations to shift taxable income from jurisdictions with relatively high tax rates to jurisdictions with relatively low tax rates in order to minimize income tax payments. For example, a foreign parent company could use internal “transfer prices” to overstate the value of the goods and services that it exports to its foreign affiliate in order to shift taxable income from the operations of the affiliate in a high-tax jurisdiction to its operations in a low-tax jurisdiction. Similarly, the foreign affiliate might understate the value of the goods and services that it exports to the parent company in order to shift taxable income from its high-tax jurisdiction to the low-tax jurisdiction of its parent. Both of these strategies would shift the company’s profits to the low-tax jurisdiction and, in doing so, reduce its worldwide tax payments. It could also be attributed to anonymity to avoid overpricing due to identification of interest of large corporate in new business area.

3.36 Companies and individuals also shift money from one country to another to diversify risk and protect their wealth against the impact of financial or political crises. A common technique used to circumvent currency restrictions is to ‘over-invoice’ imports or ‘under-invoice’ exports. The primary method used is the falsification of import and export invoices. By comparing discrepancies between the value of exports reported by a country and the value of imports reported by its key trading partners, the quantum of money transferred from that country through the use of the international trade system can be estimated.

3.37 In the case of transfer pricing, the reference to over- and under-invoicing relates to the legitimate allocation of income between related parties, rather than customs fraud. In many cases, this can also involve abuse of the financial system through fraudulent transactions involving a range of money transmission instruments, such as wire transfers. In practice, strategies to ‘launder’ money usually combine several different techniques. Often these involve abuse of both the financial and international trade systems.

<sup>17</sup> Inputs from DRI

3.38 The basic techniques of trade-based money laundering include:

- (a) **'Over-Invoicing' and 'Under-Invoicing' of Goods and Services**: Money laundering through the over-invoicing and under-invoicing of goods and services, which is one of the oldest methods of fraudulently transferring value across borders, remains a common practice today. The key element of this technique is the misrepresentation of the price of the good or service in order to transfer additional value between the importer and exporter. Over-invoicing of exports is one of the most common trade-based money laundering techniques used to move money. This reflects the fact that the primary focus of most customs agencies is to stop the importation of contraband and ensure that appropriate import duties are collected.
- (b) **Multiple-Invoicing of Goods and Services**: Another technique used to 'launder' funds involves issuing more than one invoice for the same trade transaction. By invoicing the same good or service more than once, a money launderer or terrorist financier is able to justify multiple payments for the same shipment of goods or delivery of services. Unlike over-invoicing and under-invoicing, it should be noted that there is no need for the exporter or importer to misrepresent the price of the good or service on the commercial invoice.
- (c) **Over-Shipment and Under-Shipment of Goods and Services**: In addition to manipulating export and import prices, a money launderer can overstate or understate the quantity of goods being shipped or services being provided. In the extreme, an exporter may not ship any goods at all, but simply collude with an importer to ensure that all shipping and customs documents associated with this so called "phantom shipment" are routinely processed. Banks and other financial institutions may unknowingly be involved in the provision of trade financing for these phantom shipments.
- (d) **Falsely Described Goods and Services**: In addition to manipulating export and import prices, a money launderer can misrepresent the quality or type of a good or service. For example, an exporter may ship a relatively inexpensive good and falsely invoice it as a more expensive item or an entirely different item. This creates a discrepancy between what appears on the shipping and customs documents and what is actually shipped. The use of false descriptions can also be used in the trade in services, such as financial advice, consulting services and market research.

Generally, cases of over-invoicing or under-invoicing primarily designed to gain a tax advantage are considered customs fraud as also other manifestations as above and are also scheduled offences under PMLA for laundering of money linked to cross border trade.

3.39 Misuse of export promotion schemes such as drawback, Duty Entitlement Pass Book (DEPB), Duty Free Import Authorization (DFIA), Vishesh Krishi Gram Upaj Yojana (VKGUY), etc. also lead to generation and flow of 'black' money. Several cases of forgery of export promotion scheme scrips / licences, meant to claim duty exemption in imports have been detected, which highlight another aspect of 'black' money generation and movement. Smuggling of goods and contraband items, FICN, drug trafficking, arms deals and other illegal activities thrive on 'black' money. Illegal trade and movement of such goods is facilitated by the use of black money and in turn generates more 'black' money. These activities, by their very nature, are clandestine and can only operate through the use of 'black' money. All the activities associated at each and every level of smuggling and illegal trade in such goods generate 'black' money which forms a part of the 'parallel' economy.

3.40 Indigenous manufacturing activities and units are also important areas for the generation and movement of black money. Many of the small manufacturing units are illegal and the manufacturing activity is never reported. All related transactions are in cash. Clandestine removal of goods from the Central Excise registered units and the production and distribution of goods in the unorganized sector is another source of generation of black money at the domestic level and leads to tax evasion. Misuse of CENVAT is another major area which accounts for significant evasion of tax and illegal movement of goods and generation of false invoices.

3.41 Evasion of service tax and generation and movement of money in the services sector is also an area which needs to be examined in detail. Payments for majority of the services are still made in cash and many such payments are not accounted for and no bill is issued against the provision of such services, thereby facilitating the generation and flow of 'black' money. The magnitude of 'black' money involved in such cases is expected to be huge as the sheer number of such service providers and their consumers is very large. For example, most of beauty parlors and hair cutting salons do not raise any bill against the services provided by them. Moreover, most of such services are in the unorganized sector. In cases where credit against payment of service tax cannot be claimed, the service provider and the consumer may agree to suppress the actual amount paid for providing the service. The amount over and above bill amount is thus the 'black' money generated in such transactions. For example, an architect may get into such an arrangement with a builder.

## **NPO SECTOR**

3.42 Misuse of tax exemption provisions under sections 10(21), 10(23C) & 11, and manipulations in the claims of deductions, especially under sections 35 and 80G of the Income Tax Act are among the sources of generation of black money. India is a member of the Financial Action Task Force (FATF), an intergovernmental body which develops and promotes policies to protect the global financial system against money laundering and financing of terrorism. One of the areas of focus of FATF is safeguarding Non-Profit Organisation (NPO) sector from risk and misuse in money laundering and terror financing. An NPO Sector Assessment Committee constituted under the Ministry of Finance has reviewed the existing control and legal mechanisms for the NPO Sector and suggested various measures for improvement.

## **PARTICIPATORY NOTES**

3.43 A Participatory Note (PN) is a derivative instrument issued in foreign jurisdictions, by a Foreign Institutional Investor (FII) / sub-accounts or one of its associates, against underlying Indian securities. PNs are popular among foreign investors since they allow these investors to earn returns on investment in the Indian market without undergoing the significant cost and time implications of directly investing in the India. These instruments are traded overseas outside the direct purview of Securities & Exchange Board of India (SEBI) surveillance thereby raising many apprehensions about the beneficial ownership and the nature of funds invested in these instruments. Concerns have been raised that some of the money coming into the market via PNs could be the unaccounted wealth camouflaged under the guise of FII investment. SEBI has been taking measures to ensure that PNs are not used as conduits for black money or terrorist funding. As per SEBI regulations, PNs can be issued to only those entities that are regulated by an appropriate regulator in the countries of their incorporation and are subject to compliance of "Know Your Client" norms. FIIs are also required to declare that these PNs have not been issued to Indian residents or non-resident Indians. Entities issuing PNs are required to submit to SEBI a monthly report which includes details of subscribers and details of securities underlying PNs. Though, the information sought from FIIs issuing PNs are being submitted regularly, the reporting requirements mandated by SEBI presently do not capture details of ultimate beneficial owners of these instruments.

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## IV. EXTENT OF BLACK MONEY IN INDIA AND ABROAD

### Approaches to estimating the size of the black economy

4.1 There is no uniformity of methodology or approach, or certainty of estimation relating to 'black' money. The main difficulty arises on account of the fact that the 'black' economy exists in the shadows. There is, therefore, wide variation in the figures reported as estimates are required to be made in indirect ways. The 'shadow' economy is not distinct, and the 'parallel' economy enmeshes the white economy. Different methods adopted have their own limitations.

4.2 One of the methods is the input / output method. Therefore, where the input-output ratio is known, the output can be estimated. The method consists of using this ratio along with the input to calculate the true output. When this is compared with the declared output, the difference between the true output and the declared output represents undisclosed output of the shadow economy. This method is deceptively simple and, though it may apply more appropriately to the industry sector, ignores the fast changing technological breakthroughs, which in turn contribute to the changing output input ratios. The method is difficult to apply in the context of countries where the tertiary sector grows at a faster pace compared to the primary and secondary sectors.

4.3 There is another approach – that of the monetarists, which is based on the fact that money is needed to circulate incomes in both 'black' and the 'white' economy. As the official economy is known, the difference between this amount and the money in circulation could be assumed to be the circulating 'black' component. In one model, the velocity of money (that is to say the number of times currency moves in a year) enables the estimation of income circulated annually. A comparison of this with the income captured in National Accounting System (NAS) gives the income not captured, which is the 'black' income generated. The assumption that NAS represents 'white' incomes is not always true – all incomes which are not captured in NAS are not 'black' incomes – for instance, incomes of the large unorganized sector.

4.4 The Survey Approach represents yet another method, wherein sample surveys are carried. They may be on the consumption pattern of a representative sample, which is then compared with the total consumption of the country. Sometimes, such surveys are carried to check illegal activities prevalent in a certain sample. In this method, the problems are of a truly representative sample, unambiguous set of questions, the willingness of persons in the sample size to reveal true facts implying a certain comfort level with the interviewers – as no one wants to admit any illegality before strangers.

4.5 There is also the 'fiscal approach' method, the underlying basis of which is that the economy comprises of several sectors, with each having its own sets of practices. The contribution of these sectors is separately worked, which when added would give the size of the entire 'black' economy. However, the manner of identifying the 'black component' in these sectors and assumptions suffer from inherent subjectivity of the researcher. This method has been used in various surveys.

### Estimates of Black Money

4.6 Attempts have been made in the past to quantify 'black' income in India. Broadly speaking, the estimates made so far have followed two distinct approaches:

- (i) Kaldor's approach of quantifying non-salary incomes above the exemption limit of Income-tax. The Direct Taxes Enquiry Committee (i.e. Wanchoo Committee, 1971) used this method with some modifications in the report India Tax Reform (1956), and
- (ii) Edgar L. Feige method of working out transaction-income on the basis of currency deposit ratio and deriving from it the 'black' income of the economy.

### Kaldor's report

4.7 N. Kaldor in his report<sup>18</sup> estimated the non- salary income on the basis of the break-up of national income into:

- (i) Wages and salaries,
- (ii) Income of the self-employed, and
- (iii) Profit, interest, rent etc.

4.8 Excluding wages and salaries from the contribution to net domestic product, he derived total non-salary income. For various sectors of the economy, on the basis of assumed proportions of non-salary incomes above the exemption limit, Kaldor estimated such non-salary income. An estimate of the actual non-salary income assessed to tax was made for each sector in order to arrive at the total non-salary income assessed to tax. The difference between the estimated non-salary income above the exemption limit and the actual non-salary income assessed to tax measures the size of the 'black' income.

### Wanchoo Committee's estimate

4.9 Direct Taxes Enquiry Committee<sup>19</sup> followed the method adopted by Kaldor with suitable modifications. It estimated assessable non-salary income for the year 1961-62 at Rs. 2,686 crore and non-salary income actually assessed to tax to be of the order of Rs. 1,875 crore. Accordingly, the income, which escaped income tax, was of the order of Rs.811 crore. This estimate of tax-evaded income required some adjustments because of exemptions and deductions allowed under the Income Tax Act. After making the rough adjustments, Wanchoo Committee found that *"the estimated income on which tax has been evaded (black income) would probably be Rs.700 crore and Rs.1,000 crore for the years 1961-62 and 1965-66 respectively"*. *"Projecting this estimate further to 1968-69 on the basis of percentage increase in national income from 1961-62 to 1968-69, the income on which tax was evaded for 1968-69 can be estimated at a figure of Rs.1,800 crore."*

### Rangnekar's estimate

4.10 Dr. D.K. Rangnekar, a member of the Wanchoo Committee, dissented from the estimates made by the Wanchoo Committee. According to him, tax evaded income for 1961-62 was of the order of Rs.1,150 crore, as compared to Wanchoo Committee's estimate of Rs. 811 crore. For 1965-66, it was Rs.2,350 crore, against Rs.1,000 crore estimated by the Wanchoo Committee. The projections of 'black' income for 1968-69 and 1969-70 were Rs.2,833 crore and Rs.3,080 crore respectively.

### Chopra's estimate

4.11 Mr. O.P. Chopra, a noted Economist, published a series of papers<sup>20</sup> on the subject of unaccounted income. He prepared a series of estimates of unaccounted income (black income) for a period of 17 years, i.e., 1960-61 to 1976-77. Chopra's methodology marked a significant departure from the Wanchoo Committee approach and as a consequence, he found a larger divergence in the two series from 1973 onwards when the income above the exemption limit registered a significant increase. The broad underlying assumptions of his methodology are:

- (i) Only non-salary income is concealed;
- (ii) Taxes other than income-tax are evaded and the study is restricted to only that part of income which is subject to income-tax. Thus, tax evasion which may be due to (a) non-payment or under-payment of excise duty, (b) sales-tax, (c) customs duties, or (d) substituting agricultural income for non-agricultural income, is not captured;
- (iii) The efficiency of the tax administration remains unchanged;

<sup>18</sup> India Tax Reform (1956)

<sup>19</sup> Also known as Wanchoo Committee, submitted its report in December, 1971

<sup>20</sup> Economic & Political Weekly, volume XVII, number 17 & 18 in April and May, 1982

- (iv) The ratio of non-salary income above the exemption limit to total non-salary income has remained the same; and
- (v) The ratio of non-salary income to total income accruing from various sectors of the economy remains the same.

4.12 The crucial finding of Chopra's study is that after 1973-74, the ratio of unaccounted income to assessable non-salary income has gone up, whereas the Wanchoo Committee assumed this ratio to have remained constant. As a consequence, after 1973-74, there is wide divergence between the estimates of Wanchoo Committee and those of Chopra. Chopra also corroborates the hypotheses that tax evasion is more likely to be resorted to when the rate of tax is comparatively high. His findings also support the hypothesis that increase in prices leads to an increase in unaccounted income. Further, he has given a significant finding that funds are diverted to non taxable agriculture sector, to convert unaccounted (black) income into legal (white) income. Chopra's study estimated unaccounted income to have increased from Rs.916 crore in 1960-61, i.e. 6.5% of Gross National Product (GNP) at factor cost, to Rs.8,098 crore in 1976-77 (11.4% of GNP).

### NIPFP Study on Black Economy in India

4.13 National Institute of Public Finance and Policy (NIPFP) conducted a study<sup>21</sup> under the guidance of Dr. S. Acharya. The study defines 'black' money as aggregate of incomes which is taxable but which is not reported to tax authorities. The study, however, gives a broader definition of 'black' income and calls it as "**unaccounted income**" for purposes of clarity. As there is lack of sufficient data, the NIPFP study follows "*the minimum estimate approach*" that is to say, not being able to ascertain the most probable degree of under-declaration or leakage, the study uses a degree of under-declaration which could safely be regarded as the minimum in the relevant sector. In several cases the study has also made use of a range rather than a single figure of under-estimation.

4.14 While preparing the estimate of 'black' income, the study **excludes** incomes generated through illegal activities like smuggling, black market transactions, acceptance of bribes, kickbacks, etc. To prepare a global estimate of black income, the study confines itself briefly into six areas:-

- (i) factor incomes received either openly or covertly while participating in the production of goods and services;
- (ii) 'black' income generated in relation to capital receipts on sale of asset;
- (iii) 'black' income generated in fixed capital formation in the public sector;
- (iv) 'black' income generated in relation to private corporate sector;
- (v) 'black' income generated in relation to export; and
- (vi) 'black' income generated through over-invoicing of imports by the Private sector and sale of import licenses.

4.15 After aggregating the different components of 'black' income the study quantified the extent of 'black' money for different years as under:-

Year	Estimate for black money (Rs in Crore)	%age of GDP
75-76	9,958 to 11,870	15 to 18%
80-81	20,362 to 23,678	18 to 21%
83-84	31,584 to 36,784	18 to 21%

<sup>21</sup> Study commissioned in 1983 was completed and Report submitted in March, 1985

4.16 NIPFP study concludes that “total black income generation of Rs. 36,784 crore or in round numbers Rs. 37,000 crore out of a total GDP at factor cost of Rs. 1,73,420 crore seems to be on the high side, although it turns out to be less than 30 per cent of GDP as against some extravagant estimates placing it at 50 or even 100 per cent of GDP. Taking out lower estimate, what we would say with some degree of confidence is that black income generation in the Indian economy in 1983-84 cannot be placed below 18 per cent of GDP at factor cost or 16 per cent of GDP at market prices.”

4.17 While the NIPFP Report estimates the extent of ‘black’ economy (not counting smuggling and illegal activities) at about 20% of the GDP for the year 1980-81, Shri Suraj B Gupta, a noted economist, has pointed out<sup>22</sup> some erroneous assumptions in NIPFP study. He estimated ‘black’ income as 42% of GDP for the year 1980-81 and 51% for the year 1987-88. Shri Arun Kumar in his book<sup>23</sup> has pointed out certain defects in NIPFP study and Gupta’s method. He estimated the extent of ‘black’ income to be about 35% for the year 1990-91 & 40% for the year 1995-96.

4.18 Thus, it can be said that though ‘black’ money exists to a substantial extent in our economy, its quantum cannot be determined exactly.

### International estimates of black economy

4.19 The estimates in studies done by economists employ assumptions for models, and cannot be called scientific. The ‘black’ economy exists in shadows. As the ‘shadow’ economy is enmeshed in the ‘white’ economy, the traces it leaves are used to detect and estimate the size of the ‘black’ economy by different methods, some of which have been discussed above. Each suffers from its own limitations. The last official study was done at the behest of the Ministry of Finance by NIPFP in 1985. The alternative estimates of ‘black’ income for the decade prior to 1985, compiled in the NIPFP Report (**TABLE-D1**), show the extent of variation in the estimates.

4.20 The ‘black’, ‘shadow’ or ‘underground’ economy is all the money and jobs generated outside the official economy, whether legally or illegally. A moot question may be how India compares with other countries in the world. In more than fifty countries around the world, such economy is at least forty percent the size of the documented G.D.P. Though nailing down shadowy numbers is difficult, as per Dr Friedrich Schneider of Austria’s Kepler University of Lizz, who co-authored a report<sup>24</sup> (with Claudio Montenegro of the World Bank), the margin of error factored into the reports is 15%. At one end of the scale is U.S.A., where the ‘shadow’ economy equalled only 9% of the country’s official economy. On the other end in percentage terms, the biggest ‘underground’ economy relative to the official economic activity is the former Soviet republic of Georgia, with the ‘shadow’ economy being as high as 72.5%. The higher the component of such economy, the more the Government loses on revenues it could use to improve infrastructure, reduce disparities in income and provide better education and health services. Greece has a ‘shadow’ or ‘underground’ economy equalling 31% of G.D.P. as per a later report.<sup>25</sup> One notable feature of their report is that from 1999 to 2007 ‘shadow’ economies appear to have risen for every country. The reason attributed is the increase in taxation and increasing regulations. However, in case of Peru, apparently the huge ‘shadow’ economy arose from growing urbanization and more commerce. Patently illegal activities, like drug trade, burglary, kidnappings were not included for purposes of their report. What was included was ‘all market based legal production of goods and services that are concealed from public authorities’ to avoid payment of taxes. Regardless of what taxpayers may like to believe, Schneider and co-authors suggest not merely efficient tax collecting and lighter regulation, but also to find a way to make work in the official economy more attractive and thereby reduce the incentives to participate in the shadow world.

<sup>22</sup> ‘Black Income in India’, Sage Publications (1992, first edition)

<sup>23</sup> ‘The Black Economy in India’ (1999, second edition)

<sup>24</sup> ‘Shadow Economies of 150 Countries’ – published prior to the report cited next

<sup>25</sup> Friedrich Schneider & Andreas Buehn & Claudio E. Montenegro, 2010 “Shadow Economies All over the World: New Estimates for 162 Countries from 1999 to 2007,” Working Papers wp322, University of Chile, Department of Economics

4.21 In his report, Schneider has estimated the size of 'shadow' economies using the DYMIMIC and Currency demand method for developing, emerging and developed economies. The size of 'shadow' economies of 28 Asian countries in the years 1999-00 to 2002-03 (**TABLE-D2**) shows that the 'shadow' economy in India is below the average of these countries, although the pattern of marginal annual increase of 'shadow' economy to the GDP ratio in the three years is common to most countries, including India.

### **Illicit financial flows from India**

4.22 Another important aspect which merits consideration is the illicit financial flows of 'black' money transfers from India since independence. On the one hand there has been intense speculation on illicit financial flows from India and on the other hand intense attention in the media has heightened the sense of public awareness and concern on the need to curb such generation and outflows. Though no official studies have been carried out in recent years, Dev Kar of the Global Financial Integrity Centre for International Policy, Washington estimates that since independence, a total of US \$ 213.2 billion was shifted out of India between 1948 and 2008, which constituted<sup>26</sup> 16.6% of India's GDP at the end of 2008. In his analysis, the researcher on the basis of data, confirmed that economic reforms since 1991 had led to faster growth, though such rapid economic growth in the post reform period led to more skewed income distribution. In the post reform period, the paper also indicates that faster economic growth appears to go hand in hand with larger illicit flows and worsening of income distribution. Since 1991, with more trade openness, the size of the external trade to GDP doubled from 10.8% to 21.7%, which showed statistically significant openness and was positively related to trade mis-invoicing. In the paper a simulation model identifies sets of complex drives, namely, government deficit; inflation and inflationary expectation; structural factors such as increasing trade openness, faster rates of economic growth, their impact on income distribution and overall governance captured as a measure of underground economy. Illicit flows are also driven by the desire to hide ill-gotten wealth. The corollary of increased trade liberalization provided more opportunities to related and unrelated companies to mis-invoice trade, which support the view that economic reform and liberalization is needed to be adopted with strengthened institutions and governance, if governments are to curtail capital flight. In other words, deregulation without oversight would not prevent abuse of international trade for transferring capital abroad. Kar also suggests that proposal to get money secreted abroad back into the country through amnesty for offenders to return the money by a certain date failing which a huge penalty and prosecution would follow, would be a non-starter. Such tax amnesty does nothing to encourage persons having secreted money abroad to bring it to the country as they are not subject to any tax in the first place. Any attempt to declare such illicit funds secreted abroad through an unilateral government declaration would also fall flat, as such a declaration would not materially change matters. The funds would continue to be illicit as before while their owners would continue to have access to such funds outside the country in full co-operation of secrecy jurisdictions without any knowledge of Indian authorities.

### **Study commissioned by Government of India (2011)**

4.23 The Government has commissioned fresh study on unaccounted income / wealth both inside and outside the country, bringing out the nature of activities engendering money 'laundering' and its ramifications on national security to be conducted by three national-level institutes, viz. National Institute of Public Finance and Policy (NIPFP), National Institute of Financial Management (NIFM) and National Council of Applied Economic Research (NCAER).

The terms of reference of the study are as under:

- (i) To assess/survey unaccounted income and wealth both inside and outside the country.

<sup>26</sup> An empirical study on the transfer of black money from India 1948 - 2008 – Dev Kar from Economic and Political Weekly, April 9, 2011 – Vol.XLVI No.15



- (ii) To profile the nature of activities engendering money laundering both inside and outside the country with its ramifications on national security.
- (iii) To identify important sectors of economy in which unaccounted money is generated and examine causes and conditions that result in generation of unaccounted money.
- (iv) To examine the methods employed in generation of unaccounted money and conversion of the same into accounted money.
- (v) To suggest ways and means for detection and prevention of unaccounted money and bringing the same into the mainstream of economy.
- (vi) To suggest methods to be employed for bringing to tax unaccounted money kept outside India.
- (vii) To estimate the quantum of non-payment of tax due to evasion by registered corporate bodies.

The study is expected to be completed by September 2012.

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## V. EXISTING LEGAL PROVISIONS AND ADMINISTRATIVE MACHINERY TO DEAL WITH BLACK MONEY

As the sources of generation of black money, and the forms it takes, vary, there can be no single or omnibus law to deal with the menace. The legal framework against black money generation and its control is, accordingly, dispersed in penal laws, economic laws, tax laws and various regulatory mechanisms, and the concomitant administrative machinery to enforce these laws and regulations.

### LEGAL PROVISIONS

#### 5.1 Income Tax Act, 1961

**Section 131:** The powers u/s 131 of IT Act are co-existent with that of a Civil Court trying a suit. Under Section 30 of CPC read with Rule 12, 14 & 15 of Order – XI, the powers of a court are:-

- i. Discovery and inspection - order XI
- ii. Summoning and attendance of witness - order XVI
- iii. Issue of commission to examine a witness - order XXVI ( Rules 1 to 8)

**Section 132:** Search can only be authorized by an officer of rank of Commissioner or above. Certain conditions are required to be fulfilled before authorizing a search. Powers under section 132 include power to seize books, documents, cash, jewellery, other valuables etc and the same can be retained for a certain period of time.

**Section 133A:** Survey at business premises for inspecting books of accounts, tallying stock, verification of cash, etc.

**Section 133B:** Collection of information from tax-payers.

**Section 133:** Power to requisition information from third parties.

**Section 136:** Declares income tax proceedings as judicial proceedings in case of:-

- i. Section 193 of IPC – furnishing or fabricating false evidence;
- ii. Section 196 of IPC – using evidence known to be false;
- iii. Section 228 of IPC – intentional insult or interruption to public servant sitting in a judicial proceeding;
- iv. Section 195 of Cr PC – taking cognizance of an offence of giving false evidence, fabrication of evidence, abetment or criminal conspiracy to fabricate evidence (complaint to be made to Judicial Magistrate as Chapter XXVI of Cr PC is excluded).

**Chapter XXI of the Income Tax Act, 1961:** Provides for monetary penalties at different rates for various defaults such as concealment of income; failure to comply with statutory notices, file tax returns / sign statements, maintain / retain books of account or documents, deduct / collect taxes at source; etc. Maximum penalty prescribed is 300% for the tax sought to be evaded.

**Chapter XXII of the Income Tax Act, 1961:** Provides for prosecutions against various offences such as willful evasion of tax; failure to furnish tax returns or produce accounts / documents, falsification of accounts / false statement in affidavit; failure to deduct and deposit taxes; etc. The maximum sentence is for 7 years rigorous imprisonment with fine.

#### 5.2 Wealth Tax Act, 1957

The Wealth Tax Act, 1957 contains provisions that are at par with different provisions under the Income Tax Act, 1961 as enumerated above.

### 5.3 Benami Transactions (Prohibition) Act

5.3.1 In the implementation of the Income Tax Act it was found that many persons entered into benami transactions, to distance themselves from the real transactions. A benami purchase is a purchase in name of another person, who does not pay the consideration but merely lends his name, while the control vests in another person who actually purchases the property and he is the beneficial owner. The Law Commission was requested to examine the subject of benami transactions and its ramifications. To implement the recommendations of the 57<sup>th</sup> Report of the Law Commission, the Benami Transactions (Prohibition) Bill was introduced in Parliament, which became **Benami Transactions (Prohibition) Act** after receiving assent of the President on **5<sup>th</sup> September, 1988**. The bill inter-alia provided for the following, viz.:-

- a) entering into *benami* transactions after the commencement of the new law will be an offence, with an exception for the transfer of properties by the husband or father for the benefit of the wife or unmarried daughters;
- b) all the properties *held benami* will be subject to acquisition by such authority, in such manner and after following such procedure, as may be prescribed by rules under the proposed legislation. As a result of the provisions of the Ordinance and the prohibition of entering into *benami* transactions, the *benamidar* would be acquiring the rights to the property by the mere lending of his name and without investing any money for the purchase of such property. Accordingly, it is provided that no amount shall be payable for the acquisition of any property held *benami*;
- c) Sections 81 and 94 of the Indian Trusts Act, 1882, shall also be repealed.

5.3.2 During the process of formulating the rules for implementing certain provisions of the 1988 Act, it was found that the provisions of the aforesaid Act were inadequate to deal with *benami* transactions as the Act, *inter alia*, -

- (i) did not contain any specific provision for vesting of confiscated property with the Central Government;
- (ii) did not have any provision for an appellate mechanism against an action taken by the authorities under the Act, while barring the jurisdiction of a Civil Court;
- (iii) did not confer the powers of a Civil Court upon the authorities for its implementation.

5.3.3 In view of the above, a comprehensive legislation became necessary in order to prohibit holding property in *benami* and to restrict right to recover or transfer property held *benami* and also to provide a mechanism and procedure for confiscation of property held *benami*. It was, therefore, felt necessary to repeal the 1988 Act and enact a new comprehensive legislation to deal with *benami* transactions. Accordingly, a new bill was introduced in Parliament in 2011, which is under examination of the Standing Committee. The Bill, inter-alia, provides for the following:-

- (i) it prohibits *benami* transactions by any person, except in the case of *benami* transactions entered into in the name of spouse, brother or sister or any lineal ascendant or descendant;
- (ii) it provides that *benami* property arising out of prohibited *benami* transaction is liable to confiscation by the Central Government and such property shall vest absolutely in the Central Government without paying any compensation;
- (iii) it prohibits right of the *benamidar* to recover property held *benami*;
- (iv) it provides that the Initiating Officer, the Approving Authority and the Administrator shall be the authorities for the purpose of the Bill;
- (v) it provides that the Adjudicating Authority and the Appellate Tribunal established under the Prevention of Money-Laundering Act, 2002 shall respectively be the Adjudicating Authority and

the Appellate Tribunal for the purposes of the Bill and any person aggrieved by an order of Adjudicating Authority may prefer an appeal to the Appellate Tribunal;

- (vi) it provides that any party aggrieved by any decision or order of the Appellate Tribunal may file an appeal to the High Court on any question of law;
- (vii) it enables the Central Government, in consultation with the Chief Justice of the High Court, to designate one or more Courts of Session as Special Court or Special Courts for the purpose of the Bill;
- (viii) it provides penalty for entering into prohibited *benami* transactions and for furnishing any false documents in any proceeding under the Bill;
- (ix) it provides for transfer of any suit or proceeding in respect of a *benami* transaction pending in any Court (other than High Court) or Tribunal or before any authority to the Appellate Tribunal as provided in the Bill;
- (x) it also proposes to make consequential amendments in the Prevention of Money Laundering Act, 2002.

#### 5.4 Foreign Exchange Management Act (FEMA), 2002<sup>27</sup>

Enforcement Directorate takes up investigations under FEMA in specific cases relating to contraventions in foreign exchange transactions, generally by persons resident in India. Unauthorized holding of funds outside India by any person resident in India, is a contravention of section 4 of FEMA. Upon coming to the conclusion of such a charge being established in adjudication proceedings under FEMA, in terms of section 13(1) of the Act, a suitable penalty can be imposed. Further, besides the imposition of penalty, in terms of section 13(2) of FEMA, the adjudicating authority can order confiscation of the amounts lying abroad and direct the bringing back into India of such foreign exchange holdings. FEMA is a civil law and hence no criminal prosecution can be launched.

#### 5.5 Prevention of Money Laundering Act (PMLA), 2002<sup>28</sup>

5.5.1 PMLA is a criminal law which came into force from 1.7.2005. Under the scheme of the Act, money laundering linked to the predicate scheduled offences is liable for punishment. There are 156 offences in 28 different statutes which are Scheduled Offences under PMLA. Section 3 of PMLA defines the offence of money laundering. Once the agency concerned with a predicate scheduled offence registers a case, Enforcement Directorate takes up investigations under PMLA to ascertain the proceeds of crime generated from the predicate offence booked by the Law Enforcement Agency. In case, a prima-facie case of generation of proceeds of crime and laundering thereof is made out, PMLA provides for seizure (section 17) and attachment of laundered properties (section 5). The action of seizure and attachment is required to be adjudged by the Adjudicating Authority under PMLA (section 8). The persons, both natural and legal entities, who are accused of the offence of money laundering linked to the scheduled offence can be prosecuted in Special Courts as per section 44 of PMLA. Section 4 of PMLA provides for rigorous imprisonment of minimum three years which can extend up to seven years and a fine of up to Rs.5 lakhs on conviction by the Court of persons who have been accused of the offence of money laundering. The conviction can extend up to 10 years if the offence of money laundering is linked to narcotic trafficking. The property attached under PMLA can be confiscated by the Adjudicating Authority (section 8) after the conviction by the Court of the accused in the trial for scheduled offence. In terms of PMLA, the tainted proceeds, if found parked overseas, can also be restituted through Mutual Legal Assistance after the collection of such evidence through the process of Letter of Requests with the foreign administration. Chapter IX of PMLA sets out the procedure for reciprocal arrangements with Contracting States for seizure, attachment and confiscation of assets found lying overseas. India has signed Mutual Legal Assistance Treaty (MLAT) with 26 countries and by virtue of the provisions of PMLA, Government of India

<sup>27</sup> Inputs from Directorate of Enforcement

<sup>28</sup> Inputs from Directorate of Enforcement

is fully armed with legal measures to get the tainted assets repatriated back to the country on conviction of persons accused of money laundering. Till the conviction, the assets traced overseas can be requested to be seized or frozen by foreign jurisdictions.

5.5.2 Section 12 of PMLA requires financial sector entities (banking companies, financial institutions and intermediaries) to verify the identity of their clients, maintain records and report suspicious / cash transactions (STR / CTR) to FIU-IND. Director, FIU-IND is empowered to conduct inquiry and impose sanctions against financial sector entities for non-compliance with section 12. FIU-IND conducts analysis of information received under PMLA and in appropriate cases disseminates information to relevant intelligence / enforcement agencies, which include Central Board of Direct Taxes, Central Board of Excise & Customs, Enforcement Directorate, Narcotics Control Bureau, Central Bureau of Investigation, Intelligence agencies and regulators of financial sector.

5.5.3 It may be seen that under both the Acts, i.e. FEMA and PMLA, investigation is initiated against specific persons, both natural and legal, and such action is initiated on the basis of specific information.

## 5.6 Customs & Narcotic Drugs and Psychotropic Substances (NDPS) laws<sup>29</sup>

5.6.1 The penal provisions under the Customs Act, 1962 are Section 112 (penalty for improper importation of goods), Section 114 (penalty for attempt to export goods improperly), Section 114A (penalty for short levy or non levy of duty) under which penalty equivalent to the value of the offended goods can be imposed. Under Section 114AA (penalty for use of false and incorrect material), penalty equivalent to five times of the value of the offending goods may be imposed.

5.6.2 Besides imposing penalty any person who has contravened any provision of the Customs Act, 1962, can be prosecuted for committing such offence under the provisions of Section 132 and Section 135 of the Act. Under Section 132 of the Act the offender is punishable with imprisonment for a term which may extend to two years or with fine or with both. Under Section 135 of the Act the offender is punishable with imprisonment for a term which may extend to seven years.

5.6.3 Similarly, under the Narcotic Drugs and Psychotropic Substances (NDPS) Act, 1985, stringent penal provisions exist under Section 21 to Section 32 of the Act for imprisonment varying between six months and twenty years, depending on the quantity of the contraband and seriousness of offence. In addition to this a fine may be imposed on the accused which may vary between Rs.10,000 and Rs.2,00,000. In the case of subsequent conviction death sentence can also be awarded under Section 31A of the Act.

5.6.4 The offences under the Customs Act, 1962 and the NDPS Act, 1985 are "Predicate Offence" under the PML Act, 2002. Hence the tainted proceeds acquired by contravening the provisions of the Customs Act, 1962 and the NDPS Act, 1985, can be attached and confiscated under the PML Act, 2002. The existing provisions relating to confiscation and punishments are considered adequate, but the problem is found to lie in having proper administrative framework, implementation and cooperation among various agencies.

## 5.7 Prevention of Corruption Act & United Nations Convention Against Corruption (UNCAC)

5.7.1 The Prevention of Corruption Act, 1988 (No.49 of 1988) has been enacted to consolidate and amend the law relating to the prevention of corruption and for matters connected therewith. It came into force with effect from 9th September, 1988. The maximum punishment under the P C Act is 7 years rigorous imprisonment with fine. This is less than maximum sentence of 10 years for serious fiscal crimes such as narcotics and laundering proceeds of crime.

5.7.2 India has ratified the United Nations Convention against Transnational Organised Crime and its three protocols and the United Nations Convention against Corruption. The Convention enumerates in detail the measures to prevent corruption, including the application of prevention policies and practices,

<sup>29</sup> Inputs from Directorate of Revenue Intelligence

the establishment of bodies for that purpose, the application of codes of conduct for public servants, and public procurement. It recommends promoting transparency and accountability in the management of public finances and in the private sector, with tougher accounting and auditing standards. Measures to prevent 'money-laundering' are also provided for, together with measures to secure the independence of the judiciary. Public reporting and participation of society are encouraged as preventive measures. The Convention recommends the State Parties to adopt such legislative and other measures as may be necessary to establish a whole series of criminal offences. These are:

- (i) Corruption of national or foreign public officials and officials of public international organizations;
- (ii) Embezzlement, misappropriation or other diversion by a public official of any public or private property;
- (iii) Trading in influence; and
- (iv) Abuse of functions and illicit enrichment.

5.7.3 In the private sector, the Convention calls for the creation of offences of embezzlement and corruption. There are other offences relating to 'laundering' the proceeds of crime, handling stolen property, obstructing the administration of justice, and participating in and attempting embezzlement or corruption. Following ratification of UNCAC, the Prevention of Bribery of Foreign Public Officials and Officials of Public International Organizations Bill, 2011 was introduced in the Lok Sabha on March 25, 2011. The Bill empowers the Central Government to enter into agreements with other countries (contracting states) for enforcing this law and for exchange of investigative information.

## 5.8 State laws

5.8.1 The states of the Indian Union have a wide array of powers under List-II of the Constitution to control economic activity by way of levying taxes, and secondly, by way of controlling certain industrial and commercial activities, as well as movement of goods and services.

5.8.2 Stamp duty is levied by the state governments on all transfers of immovable property. The levy of stamp duty is a State subject and thus the rates of stamp duty vary from State to State. Stamp duty is a transaction tax; it is charged as a percentage of the transaction value of the property. It varies from around 4% in Mumbai to about 13% in Kerala. Haryana charges 6% as stamp duty on properties, while it is 8% in Uttar Pradesh. Most of the states charge around 6%-8%. Circle rates basically lay down the minimum valuation of lands and immovable properties. Circle rates, as and when revised and notified by the relevant State Government, are taken into consideration by the competent registering authorities, at the time of registration of instruments relating to land and immovable properties. Lack of uniformity in stamp duty rates, which are also perceived to be high, and infrequent updating of circle rates, however, results in revenue leakages and accumulation of 'black' money in immovable property.

5.8.3 In the recent investigations by Income Tax department on the mining industry in Karnataka, it has come to light that state law allows unregistered dealers (URD) to trade in minerals, possibly as a measure to raise revenue. This is contrary to the Central Mines and Minerals (Regulation and Development) Act, 1957 and encourages illegal mining and unregulated trade in minerals. It also came to light that there was mismatch between exports and inward remittance, as also between information available with different authorities.

## ADMINISTRATIVE MACHINERY

5.9 The principal agency to tackle the generation and control of 'black' money is the Central Board of Direct Taxes (CBDT), which deals with all direct taxes. The CBDT – including its Commissionerates and Directorates of Investigation, International Taxation, Transfer Pricing, Exemption, Intelligence and Criminal

Investigation, etc. – is responsible for administration of direct tax laws; the Central Board of Excise and Customs (CBEC), including Commissionerates of Customs, Central Excise and Service Tax; DRI, DGCEI, etc., implements indirect tax laws relating to customs, central excise, service tax, etc. Other concerned agencies are: Central Bureau of Narcotics (CBN) which regulates the production and sale of narcotics; Directorate of Enforcement (ED) which enforces the Prevention of Money-Laundering (PMLA) and Foreign Exchange Management Act (FEMA); Central Economic Intelligence Bureau (CEIB) which is tasked with ensuring proper sharing and analysis of economic intelligence; and Financial Intelligence Unit (FIU-IND) which collects and analyzes data from the banking and financial sector. Other central organizations such as Narcotics Control Bureau (NCB) under the Ministry of Home Affairs; Serious Frauds Investigating Office (SFIO) and Registrars of Companies under the Ministry of Corporate Affairs; and regulators such as RBI, SEBI, FMC, IRDA, TRAI, etc., also contribute to formulation and implementation of the regulatory framework that helps check generation of black money and growth of black economy. Sales Tax departments of various state governments implement VAT in the states.

5.10 One of the principal concerns is severe shortages of manpower (Table below), particularly in the CBDT and CBEC, affecting the effective functioning of these vital bodies.

**TABLE<sup>30</sup>**

Sl.	Name of Agency	Sanctioned	Working	Shortage
1	CBDT	57,793	42,791	15,002
2	CBEC	69,164	55,419	13,745
3	CBN	1,245	777	468
4	ED*	2,064	571	1,493
5	CEIB	113	78	35
6	FIU	74	28	46

\* *The figures are not as per Performance Budget, 2011, but after sanction of additional manpower*

5.11 Effective implementation of the laws lie not only in the individual laws by the concerned agencies, but also proper inter-agency coordination especially where one law overlaps another law, and its administrative machinery affects the other. Lack of coordination, or even conflict of interest, is the second major problem to be tackled. Another area of focus for inter-agency cooperation is information-sharing. This matter is also receiving attention in many a fora<sup>31</sup> and it is noted that information exchange has to become more professional. The EIC in the Ministry of Finance oversees intelligence sharing among different central economic intelligence and enforcement agencies through CEIB and Regional Economic Intelligence Committees (REICs). We understand that recently a comprehensive review of the role of CEIB has been undertaken by an expert group, and steps are being initiated to make the central economic intelligence sharing system more effective.

5.12 Generation of black money from legitimate activities, such as businesses or professions, non-reporting of income, overstated expenses, etc., undermines the economy, its tax-base and the rule of law, and creates inequalities. The way to fight this menace is through comprehensive and better reporting mechanism, data-mining and analysis. We understand that substantial progress has been made by CBDT, CBEC and FIU in this direction, but still a lot remains to be done.

<sup>30</sup> Performance Budget, 2011

<sup>31</sup> Review of National Security 2001, Committee on CEIB, ongoing PM's review through NSCS, etc.

5.13 The Central Vigilance Commission (CVC) is the principal central government anti-corruption watchdog; with anti-corruption units of the Central Bureau of Investigation (CBI) as its principal implementing arm. Vigilance department / bureau of different state governments are anti-corruption bodies in respect of employees of the state government. In some states, the institution of the Lokayuktas is also in place. Besides these institutions, the C&AG provides oversight for the central government and central PSUs, while the State AG provides the same for the state government and its organizations. Of late, the C&AG has become proactive and as a result several 'scams' have surfaced in the public domain. However, fact remains that although the C&AG or state AGs have been functioning for several decades, leakages in public expenditure has continued unabated. Both oversight and enforcement mechanisms against corruption need to be strengthened.

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## VI. MEASURES TO TACKLE BLACK MONEY

6. There are two dimensions of the issue of black money – first, its generation and, second, its consumption and use, including laundering of black money back to mainstream economy. Dealing with this menace has to cover both these aspects. So far as generation of black money from crime or corruption is concerned, its remedy does not lie merely in legislative or enforcement domains but also in finding much deeper socio-economic solutions. We have touched upon some of these aspects. However, generation of black money from legitimate activities has been dealt with extensively, and we make several recommendations in this regard. Further, consumption and laundering of black money, if effectively tracked and controlled, may have the ‘squeeze effect’ on the overall activities resulting in creation and sustenance of black economy. While there may not be any need to have new law to especially deal with black money and black economy, various existing laws need to be comprehensively reviewed by the concerned administrative ministries on a regular basis keeping in view the changing economic scenario, and provisions dealing with violations need to be strengthened accordingly.

### Strategy to tackle black money

The Committee has identified following strategy to tackle black money:-

- ☐ Preventing generation of black money
- ☐ Discouraging use of black money
- ☐ Effective detection of black money
- ☐ Effective investigation & adjudication
- ☐ Other steps

### Preventing generation of black money

6.1 India must ensure transparent, time-bound & better regulated approvals / permits, single window delivery of services to the extent possible and speedier judicial processes. The Electronic Delivery of Services Bill, 2011 that seeks to provide for electronic delivery of public services by the government to all persons to ensure transparency, efficiency, accountability, accessibility and reliability in delivery of such services has been tabled before the Parliament in December, 2011.

6.2 The fight against the monstrosity 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 & wasteful consumption / expenditure, encourage savings, frugality and simplicity, and reduce the gap between the rich and the poor.

6.3 The Government is also considering legislating public procurement law. The Public Procurement Bill, 2012 intends to regulate public procurement by all ministries and central government departments. It aims at ensuring transparency, fair and equitable treatment of bidders, promote competition, and enhance efficiency and economy in the public procurement process.

6.4 In order to ensure transparent and efficient allocation of natural and man-made resources, oversight in the form of comprehensive regulations and ombudsman for grievance redressal, particularly for scarce resources – as in land, minerals, forests, telecom, etc. – need to be introduced and implemented expeditiously.

6.5 Social sector schemes involving huge public expenditure under various programmes reportedly suffer from possible manipulations and leakages. Direct transfers to the accounts of beneficiaries can provide a solution, as it would prevent manipulations like bogus muster rolls, etc. While efforts such as

UID and direct transfer of subsidies will stop leakages in some sectors, in other sectors the problem will have to be addressed differently. We, accordingly, recommend that social audit be made mandatory for all social sector schemes that do not involve direct transfer of credit to the bank account of the beneficiary, at the district / field level, and a second and subsequent AG audit at the HQ level. We also recommend that a system of random inspections by teams of sponsoring Ministry / Department / Agency may monitor utilization of public funds for social sector schemes.

6.6 There should be a dedicated training center for all law enforcement agencies dealing with financial crimes and offences, as this requires special skills. A delegation from the CBDT had recently visited USA and studied the training methodology of the Federal Law Enforcement Training Center (FLETC), Brunswick GA. A multi-disciplinary institution for training in investigation of financial crimes may be established on the lines of FLETC of USA.

6.7 Oversight in the private sector is almost absent, except for some professionally managed companies. It mainly consists of self-regulation, and audit under the Company and Income Tax laws. That the system of professional audit may be quite ineffective even in professionally managed enterprises is aptly demonstrated by the Satyam case. We are of the view that the burden of dual audit should be reduced to single audit (for both company and tax law) and the audit system be detached from the management and control of the business. We, therefore, recommend that the central government establish a regulator (under Company law / Income Tax law) to empanel auditors in different grades and randomly assign them to the private sector firms, based on category and payment capacity, with mandatory rotation and maximum tenure of two years.

6.8 The proposed national level GST regime should be expeditiously implemented, as the spin-off from its implementation would provide adequate resources to more than compensate the loss apprehended by certain state governments.

6.9 At present, no government agency has complete database of NPOs. CBDT has the largest database about this sector. There may be information with other agencies such as MHA, CEIB, etc. It is desirable that CBDT be assigned the role of a centralized agency with which every NPO would require to be registered and would be allotted a unique number. This would be in line with the decision taken by the Government in the light of possible misuse of the sector in undesirable activities. There are suggestions made by the NPO Sector Assessment Committee, an Inter-ministerial body, which should be accepted and the office of DGIT (Exemption) appropriately strengthened in terms of manpower, infrastructure and capacity building.

6.10 There should also be sharing of real-time data under Foreign Contribution Regulation Act (FCRA) and DGIT (Exemption) and coordination amongst various enforcement agencies. The registration under section 12AA and approvals under sections 10(23C) / 10(21) / 35 / 80G of the Income Tax Act for charitable organizations are required to be in accordance with international best practices. For this purpose, the Income Tax Department should devise a mechanism to facilitate effective monitoring and better control over the tax administration of NPOs through modification in existing procedure of granting registrations or according approvals by allotting a PAN-linked system-generated specific number, making mandatory the quoting of this number in the tax returns and devising suitable changes in the existing tax return forms. This would filter out bogus claims and would also help in maintaining authentic data base of NPOs.

6.11 Accountability of both public and private offices needs to be enhanced. As we are mainly concerned here with public sector accountability, we recommend that apart from good practices being followed such as Fiscal Responsibility and Budget Management (FRBM) Act and outcome budget, performance-linked appraisal system of rewards and punishments, already under consideration, should be expeditiously implemented.

6.12 In the recent investigations by Income Tax department on the mining industry in Karnataka, it has come to light that state law allows unregistered dealers (URD) to trade in minerals, possibly as a measure

to raise revenue. This is contrary to the central Mines and Minerals (Regulation and Development) Act, 1957 and encourages illegal mining and unregulated trade in minerals. This situation requires immediate remedy and all laws relating to licensing and regulation in mining need a thorough review. It also came to light that there was mismatch between exports and inward remittance, as also between information available with different authorities. The anomaly between the central and the state laws with regard to URDs should be immediately removed.

### **Discouraging use of black money**

6.13 Government may consider amending existing laws (The Coinage Act 2011, The Reserve Bank of India Act 1934, FEMA, IPC, Cr PC, etc.), or enacting a new law, for regulating the possession and transportation of cash, particularly putting a limitation on cash holdings for private use, and including provisions for confiscation of cash held beyond prescribed limits. This would address the concerns expressed by various courts, and also the Election Commission of India for reducing the influence of money power during elections.

6.14 To reduce the element of black money in transactions relating to immovable properties, provision for NOC should be introduced in the Income Tax law with safeguards to reduce administrative complications and increased ease of compliance, so that an appropriate and uniform data-base is also set up, and a proper national-level regulation is put in place. The new system should be computer driven with minimal interface between the tax authorities and the tax-payer, and enforced by a dedicated unit within the investigative machinery of the Income Tax Department on the basis of pre-determined parameters and standard operating procedures. The electronically generated NOC, within a specified period, would also act as a tax clearance certificate.

6.15 The Accounting Standard No.7 should be modified by the ICAI to be made applicable to real estate developers also. AS-7 and AS-9 should be notified under the Income Tax Act, 1961.

6.16 There is no uniformity in the matter of levy of agricultural income tax among states. Agriculture generates around 14 per cent<sup>32</sup> of the country's GDP. Giving credit to agricultural income for income tax purposes without verification of claim allows an avenue for bringing black money into the financial system as agricultural income. State governments may consider levy of agricultural income tax with facility for computerized processing and selective verification. This will on the one hand enhance revenues of state governments, and on the other hand prevent laundering of black money in the garb of agricultural income.

### **Effective detection of black money**

6.17 The regulation and enforcement of KYC norms in the co-operative sector may be strengthened by the State Governments as well as the Central Government. Responsibility may be fixed for any lapse in this regard, as well as for any subsequent failure to alert authorities as regards any suspicious transactions in such accounts.

6.18 The RBI could consider stricter implementation of KYC norms and limit number of accounts that can be introduced by a single person, the number of accounts that can be maintained in the same branch by any entity and alerts about same address being used for opening accounts in different names. Stricter adherence to, and enforcement of, KYC norms is needed for ensuring proper compliance by banks and financial institutions. The Government, as well as the RBI, also need to put a better regulatory framework in place and act promptly against errant persons / institutions.

6.19 The Ministry of Corporate Affairs, which already has a centralized data-base of all companies, may examine placing a cap on the number of companies operating from the same premises and number of companies in which a person can become director.

<sup>32</sup> 2010-11, Economic Survey, 2012

6.20 The government may consider introducing alternative financial instruments to reduce the attraction of gold as savings instrument. It may also consider revising customs duties, as also graded wealth tax, on gold and jewellery to discourage investments in unproductive assets. The taxation structure on bullion and jewellery, including VAT / Sales Tax should be harmonized.

6.21 Better reporting / monitoring systems are to be put in place to trace the dealings in bullion / jewellery through the Income Tax / Customs / Sales Tax Acts. While the Income Tax Department has made it mandatory to obtain PAN or Form-60 / Form-61 for purchase of bullion above Rs.5 lakh, similar rules should be framed for purchase / sale of bullion / jewellery, and collection of tax at source on purchases especially in cash.

6.22 Use of banking channels and credit / debit cards should be encouraged, while trade practices such as cheque discounting should be discouraged. The validity period of cheques / DDs has been reduced from 6 to 3 months w.e.f. 1<sup>st</sup> April 2012, which will discourage discounting of negotiable instruments. Payments by debit / credit cards through e-service intermediaries will simplify and encourage payments in these modes and reduce the cash economy. It is imperative that payment of wages and salaries in the private sector should also be through banking channels and become cash-less, in line with the government objective of financial inclusion.

6.23 Income Tax Department, which has a large data-base of financial transactions, should immediately set up the Directorate of Risk Management for proper data mining and risk analysis. The third-party reporting mechanism of the Income Tax Department should be made computer-driven and cover most high-value transactions in the financial sector.

6.24 Foreign remittances using corporate structures and the formal financial sector instruments may be a popular method of transferring funds (even of illegal origin) to foreign jurisdictions or for routing back to India through Foreign Institutional Investors (FII). There is a need to create a robust database of such remittances and carry out an analysis of their backward and forward linkages in order to understand the nature and legitimacy of the transmitted funds. FIU-IND may be empowered by law to receive reports (similar to other reports submitted to FIU-IND) on all international fund-transfers through the Indian financial system. The FIUs of Australia and Canada are already mandated to receive such reports.

6.25 SEBI by a circular issued in January 2011 has introduced changes in the reporting formats that capture details of downstream issuances of PNs during the month. From March 2012, these detailed reports are to be filed on a monthly basis but have a lag of six months. Though such details would be useful in identifying suspicious transactions, the six month lag in the information available is likely to reduce the strength of corrective action that can be taken by SEBI. These regulations need to be modified to ensure that information on downstream issuances is collected for the most recent month. This would ensure active surveillance and timely intervention as and when required by SEBI. Further, the most critical feature of an effective monitoring mechanism lies in ensuring strict KYC norms. PN subscribers should be subject to KYC norms of either the home country or the host country whichever is stricter. Though such provision implicitly exists in the extant provisions, these need to be built into SEBI regulations explicitly for better compliance.

6.26 The oversight mechanism for the financial markets must have trained manpower with proper domain knowledge of financial investigation. This will involve placing officials from the financial investigative agencies in the operations / vigilance machinery of the banks and financial institutions to keep proper vigil and ensure that rules and regulations are followed in the banks and other financial institutions.

6.27 Foreign entities – banks, financial institutions, fund transfer entities, etc. – have set up businesses in India. It has been found that Indian tax residents have been having substantial monetary transactions through these entities or with their branches abroad. Some countries have implemented laws to make it obligatory to furnish information of all transactions undertaken abroad. We recommend that India may

also insist on entities operating in India to report all global transactions above a threshold limit. For this purpose, appropriate law, rules or contractual / licensing arrangement with these entities may be framed and implemented.

6.28 In India, there is no law to protect informants / whistle-blowers, nor does any department have effective witness protection program. As a result, credible information is not forthcoming and witnesses either do not turn up or turn hostile resulting in acquittals in prosecution cases. Apparently, the National Investigative Agency runs a program, and the recently created Directorate of Criminal Investigation (DCI) in the CBDT has been empowered to run such a program. Accordingly, we recommend that a witness protection law may be enacted expeditiously and witness protection program should be implemented by all law enforcement agencies.

6.29 DRI maintains constant interaction with its Customs Overseas Intelligence Network (COIN) offices to share intelligence and information through Diplomatic channels on the suspected import / export transactions to establish cases of mis-declaration, which are intricately linked with tax evasion and money laundering. The scope and reach of COIN offices should be further expanded and strengthened. Customs officers should be stationed in major trading partner countries to liaise with customs authorities of those countries and cause verifications of suspicious trade transactions.

6.30 Institutions of the Lok Pal and Lokayukta may be put in place at the earliest, in the centre and states, respectively, to expedite investigations into cases of corruption and bring the guilty to justice.

### **Effective investigation & adjudication**

6.31 Government must consider ways to mitigate the manpower shortage issues which are seriously hampering the functioning of various agencies particularly the CBDT and CBEC. Further, both Boards have submitted proposals for restructuring of their respective field formations. These need to be taken up and implemented on a fast track basis to show the Government's resolve to tackle the issue of black money.

6.32 Simultaneously, more administrative and financial autonomy must be expeditiously devolved on CBDT and CBEC for formulating tax policies in keeping with the overall government views on economic growth and development, for better tax administration and for providing tax-payer services as per best international practices. This has consistently been recommended by many earlier Committees<sup>33</sup> and Commissions on Tax Administration.

6.33 With the emergence of complex legal matrix, infraction of one law invariably leads to infraction of another. Inter-agency coordination is critical in the fight against black money. There is a need to evolve an effective coordination mechanism that identifies the laws violated, the law violators, and a permanent joint mechanism to investigate all such cases. Some developed countries have an approach of joint task force and de-confliction programs to deal with this issue. It is time we study how this approach and program functions, adapt it to Indian conditions and implement it.

6.34 The information and intelligence gathering mechanisms of various economic agencies need to be more broad-based so that the entire gamut of economic activity is captured in an electronic manner, mined and analyzed. All the agencies need to continuously get technologically upgraded in this area to effectively tackle the menace of black money. The skills of manpower resources available with the agencies also need to be upgraded continuously and exposed to the global best practices in their sphere of work.

6.35 Intelligence sharing is one of the most critical areas for effective law enforcement. For this purpose, there should be a platform for more effective sharing of intelligence / information between central and

<sup>33</sup> Report of the Task Force on Direct Taxes headed Dr Vijay L. Kelkar, 2002; Tax Advisory Group headed by Dr. P. Shome (2001); Chelliah Committee (1991-93); Choksi Committee (1978); Wanchoo Committee (1971)

state agencies. Information exchange among various economic law enforcement / intelligence organizations should become technology driven, preferably through a common technology platform. At the same time data-security should be ensured to prevent unauthorized access to information both technologically and through access control, and periodical security audit.

6.36 For curtailing TBML, there should be institutional arrangement for examining cases of mismatch between export and corresponding import data, as done by the Data Analysis & Research for Trade Transparency System (DARTTS) of US Customs. Indian Customs should set up a Trade Transparency Unit (TTU) on these lines for which appropriate legal framework may be introduced. Existing Customs Cooperation Agreements mostly provide for mutual administrative assistance in individual cases under investigation. These agreements should have institutional arrangement for exchange of Harmonized System of Nomenclature (HSN) chapter-wise data of export and import. Similar arrangements should be made for Preferential Trade Agreements (PTA) and Free Trade Agreements (FTA).

6.37 Effective battle against black money cannot be ensured unless the judicial machinery to deal with it is specialized and the trial of offences is expeditious and punishments exemplary. The legal support to various law enforcement agencies should be enhanced. All financial offences should be tried through fast track special courts. The Ministry of Law should take up this issue on priority and make arrangements for setting up fast-track courts all over the country in a time-bound manner. Judicial officers may be provided inputs as required in technical aspects of economic offences.

6.38 Diverse activities are covered by 'primary' enactments to regulate sale receipts, actual production, charging amount in excess of statutory amounts, etc. In some cases, investigation by income tax authorities reveals infringement of state laws. In such cases, the courts admit evidence 'accepted' by state authorities. Provision may be considered for enactment in the law of evidence or the income-tax law to the effect that even if evidence is produced under the primary law, where no independent verification is made, it will not be conclusive proof for tax purposes.

6.39 Small 'entry operators' / 'bill masters' help launder large sums of money at miniscule commissions. The appellate tax bodies tend to tax their income at nominal rates. There is no effective deterrence except for taxing commission on such bogus receipts. Taxing the entry amounts in the hands of beneficiaries usually does not stand judicial scrutiny. The amendments proposed in the Finance Bill 2012 are expected to take care of the issue in the hands of the beneficiaries. Therefore, the offence of providing fake bills and entries should be dealt with firmly.

6.40 As taxation is a highly specialized subject, most reversals in court rulings are to be found in tax jurisprudence. Government may consider creating an all-India judicial service for specialized judiciary in different laws to achieve uniformity of application.

6.41 The National Tax Tribunal is yet to come into existence. Rapidly developing specialized institutions with requisite domain knowledge, to deal with complex problems confronting the country, is a priority. A professional National Tax Tribunal, with representation from the tax administration also, should be immediately formed to deal with all tax litigation.

6.42 Improvements in the matter of reporting, analysis and communication need to be achieved by further upgrading the computerization programme of the judicial system. It will enable the law enforcement agencies in taking well informed decisions.

6.43 We further recommend that for criminal trial of economic offences, the High Courts may consider setting up exclusive economic offences courts with special summary procedure. Judicial officers posted in these courts could take refresher courses in taxation laws to properly equip them in dealing with complex tax cases.

6.44 Under economic laws, different punishments are prescribed for different offences (**TABLE-F1**). Minimum punishments should also be prescribed for economic offences, to have greater deterrence.

Different law enforcement agencies may consider lowering the punishment of 3 years to 2 years to facilitate speedier trial through summary procedure. Maximum punishments under the NDPS Act are 10 and 20 years. Under the NDPS Act, a second serious offence is punishable with death. Certainly, corruption cannot be treated as less diabolical than drug-related offences or money-laundering. Therefore, maximum punishment in serious cases of corruption should be enhanced to 10 years. Similarly, the minimum punishment for different offences of corruption should be enhanced from present 6 months, 1 year and 2 years to 1 year, 2 years and 3 years – at par with PMLA or Customs Act. Enhanced punishment, at par with other serious economic offences, is likely to provide more effective deterrence against corruption. Gist of recommendations in this regard is at **TABLE-F2**.

### Other steps

6.45 Directorate of Currency (DoC) may be strengthened to introduce coins and currencies that would be machine readable, to enable routing of cash transactions through banks easy, user-friendly and reduce the menace of FICN. This will go a long way in enabling the banks to not discourage cash deposits, thus reducing cash economy. The DoC needs to be strengthened to achieve these objectives.

6.46 To prevent misuse of 'off-market', and 'Dabba-trading' or trading outside the recognized stock exchanges, amendment to income tax law may be introduced to allow losses in off-market share transactions to be set off only against profits derived from such transactions.

6.47 As housing finance companies and the property buyers are provided fiscal incentives, it also leads to speculation and flipping transactions. To prevent this, Section 54 of the Income Tax Act should be amended to provide for availing this benefit only twice by a taxpayer in his lifetime.

6.48 The period of limitation for reopening income tax assessments should be enhanced from present six years to sixteen years for bringing to tax undisclosed assets held abroad.

6.49 One of the ways to get assets / money held abroad into the national mainstream is through a compliance scheme. The Committee is of the view that if the above recommendations are implemented properly, it would be possible to get information regarding assets held abroad as well as check the generation of black money within the country and its illicit transfer abroad. Already there are provisions in the Income Tax Act to waive prosecution and reduce penalties in genuine cases of inadvertent infraction of tax laws. Such taxpayers can always avail of the benefits under these provisions and declare any undisclosed income / assets in India or abroad.

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## VII. CONCLUSION

7.1 As regards the specific mandate assigned to the Committee, the Committee is of the view that there exists legal framework to handle undisclosed assets, irrespective of the fact whether these assets are located within or outside India. In the cases where assets have been acquired by way of illegal means, a penal offence is committed under the concerned law, and there are provisions for confiscation of such proceeds of crime, and also punishment relating thereto, under the specific law, as also under Cr PC. Any attempt to launder proceeds of crime as genuine income is a predicate offence under the PMLA and there are provisions for confiscation of assets at this stage also. The provisions of PMLA, as well as the respective laws under which the crime has been committed also provide for suitable punishment to perpetrators of such offences. In this view of the matter, no purpose will be served by declaring wealth generated illegally as national asset.

7.2 In respect of the assets acquired by Indian nationals / tax residents through legal means but not disclosed to the tax authorities in India, such assets / investments can be brought to tax under the provisions of the Income Tax Act provided requisite information in this regard is available with the Income Tax Department. In such cases, in addition to tax and interest charged, penalty for concealment of income is levied up to 300% of tax sought to be evaded. Prosecution for concealment of income is also launched in appropriate cases. The gross amount of tax, interest and penalty in most such cases equals, or even exceeds, the value of the asset / investment, thus resulting in realization of the entire evaded amount as tax revenue. This has the same effect as confiscation of undisclosed asset / income / proceeds of crime, and is applicable in cases of undisclosed assets / investments located both within and outside India.

7.3 Similarly, amounts held overseas unauthorizedly by any person resident in India can be effectively dealt with under FEMA.

7.4 Considering views / suggestions / recommendations from all the stakeholders, including the public, the Committee is of the view that there is no dearth of laws to deal with the menace of black money. However, some new laws, such as to regulate the cash economy, and some changes to the existing legal provisions also need consideration, as suggested by various stakeholders. There are multiple administrative agencies to deal with the problem of black money. There is, thus, no need to create any further agencies. However, the existing agencies need to be strengthened, both in terms of manpower and other resources. There is also a need for better coordination among all agencies.

7.5 The Union Budget 2012 has since been presented before the Parliament by the Hon'ble Finance Minister Shri Pranab Kumar Mukherjee on 16<sup>th</sup> March, 2012. Many of the suggestions placed before the Committee by the participating agencies have been given effect to in the Finance Bill, 2012. A summary of such proposals already brought in through the Finance Bill is at **ANNEX-G1**.

7.6 The Committee expresses its gratitude to the Chair and Members, both present and past (list of past Chair / Co-Chair / Members at **ANNEX-G2**), and their respective support teams, for giving valuable inputs in understanding various dimensions of the problem of black money and arriving at its several recommendations.

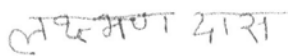
7.7 The response from the public was overwhelming, and along with industry associations such as FICCI and ASSOCHAM, contained many valuable suggestions. The Committee thanks them for their inputs, most of which find mention in this report.

7.8 The Committee also expresses its gratitude to Shri T K Shah, Chief Commissioner of Income Tax, Mumbai, for his efforts in preparing a background paper and compiling inputs from the field officers of the Income Tax department. The contribution of Investigation-I Branch and FT&TR Division of CBDT, and the FIU-IND team, to this report has been seminal.

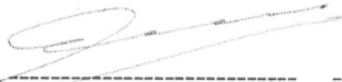


**Government of India / Ministry of Finance**  
**Report of the Committee on Black Money, 2012**  
**Headed by the Chairman, CBDT**

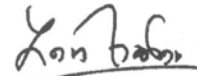
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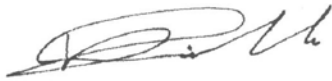
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(Laxman Das)  
Chairman



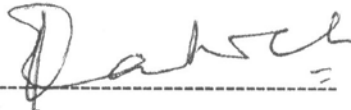
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(K M Nair)  
Co-Chair



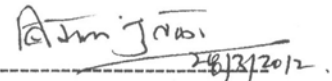
(डा. पी के सक्सेना)  
(Dr P K Saxena)  
Member



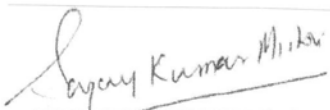
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(R S Sidhu)  
Member



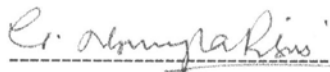
(डा. राजन कटोच)  
(Dr Rajan Katoch)  
Member

 28/3/2012

(बिमल जुल्का)  
(Bimal Julka)  
Member



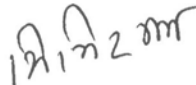
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(S K Mishra)  
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(डा. जी नारायण राजू)  
(Dr G Narayana Raju)  
Member



(पी के तिवारी)  
(P K Tiwari)  
Member



(शिशिर झा)  
(Shishir Jha)  
Member Secretary

# Part-II

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## ANNEX-A

### SUGGESTIONS ON CURBING GENERATION OF BLACK MONEY

Black money is generated through activities both legal and illegal. To check generation of black money through illegal activities, measures have to be taken to reduce and punish such activities. Although tax administrations have a limited role in checking illegal activities, the consumption and laundering of black money so generated, as well as generation of black money earned through legal means, can be checked and reduced by an efficient and alert tax administration. In this chapter, our recommendations touch upon both these areas.

1.2 Of commerce, corruption and crime – the three kinds of activities that generate black money, the first two are of greater immediate concern in India. The generation of black money in regular economic and commercial activities has two dimensions – generation of black money within the national economy and its consumption within the country; and generation of black money within the country and its transfer outside the country. It is to be noted that money illicitly transferred outside does not stay permanently abroad, as commonly believed, but is also brought back into the country in various forms. Black money generated out of corruption – whether in the public sector emanating from controls, licensing, contract or delivery of goods and services; or in the private sector originating from project financing, pilferage of public goods and services, bogus claims of expenses, under-reporting of production and sales, etc. – has to be dealt with differently and is strictly not within the purview of this Committee. However, through the anti-money-laundering and tax laws, generation of black money through corruption can be dealt with. While registration of an offence under the PC Act already constitutes an offence under the provisions for PMLA, there is scope for further introducing or modifying tax laws to track the illicit proceeds of corruption and make its consumption or laundering more difficult.

1.3 Some of the recommendations of the earlier committees/groups/studies/experts are as under:-

#### **NIPFP Study Report (1985)**

2.1 The report made recommendations covering four major areas, viz.

- (i) changes in economic and related policies designed to reduce black income generation;
- (ii) policies designed to promote integrity and improve honesty among at least senior tax officials and those dealing with controls;
- (iii) measures designed to bring down the amount of black wealth currently held; and
- (iv) policies relating to administration and enforcement of taxes, prosecution of tax offenders and imposition of penalties for economic crimes.

2.2 Among changes in economic policies, the Study recommended reduction in tax rates and simplification of the tax structure; reduction in the complexity and number of controls through de-regulation, decontrol and dependence on pricing mechanism; and proper financing of election expenses. To improve public administration, the Study recommended implementing a system of rewards for hard-work and honesty and punishment for dishonesty and negligence, along with better remuneration for public servants. Towards measures to bring down black wealth currently held, a National Fund for socially relevant projects such as slum-improvement and a voluntary disclosure scheme with immunity from prosecution were recommended. To improve tax administration, introduction of modern technology, increasing strength of the tax department and better training for its officials were recommended. For better enforcement of tax laws and prosecution of tax offenders, the recommendations made included reduction in number of scrutinizes and searches; increase in number of surveys; quick disposal of assessments, imposition of penalties and launching of prosecution in search cases; amendments to Chapter-XXA to make it more effective in dealing with generation of black money in immovable property transactions; shifting the initial burden of proof on the tax evader; and setting up special courts to try tax and other economic offences with special and speedier trials.

### **Suraj B Gupta 'Black Income in India' (1992)**

2.3 In his study published by Sage as above, Mr Suraj Gupta criticized the earlier measures undertaken by the government from time to time to unearth black money, viz. VDI Schemes 1951, 1965, 1975 and 1985; SBB Scheme 1981; and demonetization of currency in 1946 and 1978; and also touched upon the schemes launched by the government during 1991-92. His critique of improper implementation of statutory tax provisions; ineffective surveys, search and seizures; imposition of few penalties and rare prosecutions due to legal interpretations and delays; appear to indicate that dealing with the menace of black money was more an implementation issue.

### **Arun Kumar 'The Black Economy in India' (1999)**

2.4 In his study published by Penguin as above, while Mr Arun Kumar did criticize as failures the following measures undertaken from time to time to tackle black money – (a) voluntary disclosure schemes; (b) demonetization in the year 1978; and (c) lowering of tax rates; he recommended better regulation of real estate and financial markets, right to information, as well as political and judicial reforms to reduce the need to generate and curb black wealth.

### **Vijay Kelkar Task Force (2003)**

2.5 According to the Kelkar Task Force (KTF), the fundamental role of tax administration is, to render quality taxpayer services to encourage voluntary compliance of tax laws, and to detect and penalise non-compliance. Recommending introduction of best international practices in the area of taxpayer services for widening the tax base through voluntary compliance, most of the measures recommended by KTF are under various stages of implementation or stand implemented (**TABLE-H1**). In the area of personal and corporate taxation, KTF had made a number of recommendations with a view to reduce the tax slabs, deductions and exemptions. Most of these recommendations have also been either implemented or are in the process of implementation, primarily through the Direct Taxes Code Bill 2010 (**TABLE-H2**).

## **INCOME TAX DEPARTMENT**

### **Real Estate**

3.1 Real estate is one the biggest source and mode of consumption of black money. There are no provisions in the Act to effectively counter this menace. The valuation adopted by stamp authorities is in most cases completely out of line with the prevailing market value and the provisions of Section 50C, introduced by the Finance Act, 2002 (w.e.f. 1.4.2003), mandates that the stamp value is to be taken as the value of sale consideration of property. In several cases, transactions for transfer of property are arranged in such a way that there is no registration before the Stamp Valuation Authority as on the date of transfer. In such cases, provisions of Section 50C cannot be invoked. In fact, black money used in purchases is entirely outside the scheme u/s 50C.

3.2 Earlier Chapter XX-C of the Income Tax Act, 1961 provided for presumptive purchase by the Central Government, in cases where properties were grossly undervalued. However, the Chapter ceased to apply on and after 1st July, 2002. Mostly, the stamp duty rates are fixed in an extremely general manner. The present arrangement is therefore not satisfactory in curbing both the generation and utilization of black money. Suitable methodology and appropriate authority needs to be created for fixing the rates of the property of particular areas and periodically revaluation of the same keeping in view the market conditions. The earlier system of the government buying such land at the agreed consideration plus a reasonable profit could be brought back with improvements. It may be worthwhile to create a new Directorate for this purpose, as an Acquisition Wing of the Income Tax Department.

3.3 Acquisition of land by cash payment has the consequence of facilitating routing of black incomes and as farmers move elsewhere, chargeability of capital gains on sellers, i.e. farmers, cannot be enforced. Section 194LA, providing for tax deduction at 10% of the consideration paid enabled monitoring of such transactions. This has encouraged large cash payments to farmers. The provision was not made applicable to agricultural land. It would be in the interest of farmers if they received payment through bank instruments, as savings in banks would be safer than handling cash before transferring it to a bank.

3.4 With the continuous rise in prices along with fiscal benefits on residential properties, high-net worth individuals are motivated not by a need to build properties but invest in properties, only with a view to transferring them and encashing the 'gain' as capital gain. As housing finance and the property buyers are provided fiscal incentives, provisions like Section 54, 54EA and 54F of the Income Tax Act need to be amended to extend the holding period to five years, to reduce 'flipping' of properties, and thereby speculation.

3.5 Often, properties are owned by public limited companies in which public are not substantially interested. These are generally old properties, whose value has appreciated manifold over years but, the book value of the property is shown at the original market price, a pittance compared to its market value as on date. In such cases, properties are transferred through transfer of shares of the companies owning them. Since, the book value of the property is very low, the purchaser only pays for the shares of the company by cheque and the remaining part of the consideration in respect of property transfer, is paid as per current market value, in cash. It is suggested that IT Dept bring in appropriate legislative changes to curb use of black money in such transactions:

- (a) When 25% shares of a company, in which public are not interested, are transferred in a financial year, the total assets of the company must be revalued as per circle rate/rate adopted by the 'Registration Authority'. Artefacts, antiques, paintings must also be revalued by authorized valuer.
- (b) Shares of the subsidiary company will also be required to be re-valued in such cases, as per the method mentioned above.
- (c) The capital gains arising taking the book value as sale consideration should be taxed in the hands of the seller.
- (d) Stamp duty should also be charged treating such transfer of share as transfer of property.

3.6 Immovable properties of substantial worth are sometimes being transferred indirectly, by way of transfer of shares/stake of the company/concern, which is the owner of property. Such transactions result in evasion of Capital Gains tax and also avoidance of substantial amount of Stamp duty. There should be specific provision in Income tax Act to ascertain the market value of shares of company, based on the prevailing market price of the properties held by the company.

3.7 The clause (iii) of Section 2(14) gives definition of agricultural land for capital gains purposes and as per the existing definition, lands situated beyond 8 Kms from local limits of the municipal area are excluded from the ambit of capital gains. In view of the rapid urbanisation, urban limit should be extended from existing 8 Kms of municipal area and sale of agricultural land to a non-agriculturist or for non-agricultural use should be subject to tax mandatorily.

### **Bullion & Jewellery**

3.8 India is one of the largest importers and consumer of gold in the world and its demand per annum is around 850 metric tonnes. Of late it is seen that investment of black money in bullion has increased, leading to spurt in bullion prices. The Government may consider introducing inflation-linked bonds to reduce the attraction of gold/silver as savings investment. It may also consider revising custom duties as also wealth tax on gold and jewellery, to discourage such purchases by households. To curb such incidences, the following legislative changes may be considered:

- (a) Import duty on purchase of gold should be increased from \$ 200 per 10 gm to 5% of total cost and exporter of jewellery should get import benefit on export of jewellery.
- (b) All transactions in bullion of more than one lakh should be by Account Payee Cheque only.
- (c) If any unexplained bullion/jewellery is found during the course of search, mandatory penalty @ 300% u/s 271(1)(c) should be imposable.

## Capital Markets

3.9 Long term capital gain on sale of certain financial assets is subject to no or nominal tax. This provides an opportunity to launder money as sale proceeds of such assets by paying no or minimal tax. The rate of tax for capital gain and income from business should be uniform to reduce the element of tax arbitrage.

3.10 There is a common *modus operandi* adopted by many private companies for introduction of black money, i.e. by way of share application money, share capital or unsecured loan. The idle share application money is just like unsecured loan but without interest. Suitable amendment to the Income Tax Act may be introduced to impose presumptive tax on the total amount of money collected by way share application money if they are not allotted within a certain time period or refunded. This will stop the tendency to introduce unaccounted money through this method.

3.11 Promoters of listed companies adopt dubious methods to jack up prices of shares which are then off-loaded. Later, as prices crash shares are re-purchased at lower value by them or through controlled shell entities. This cycle goes on and provides opportunities for purchase of losses and set off incomes/gains. As per Section 10(38) of Income Tax Act, income arising from the transfer of a long-term capital asset, being an equity share in a company is exempt. This provision needs to be reviewed. The exemption should be given up to a certain limit to give benefit to small investors.

3.12 A large portion of the black money which goes out of the country is believed to come back as investment in Indian businesses from tax havens in the form of share capital/share premium/share application money from the local market, or as Foreign Direct Investment (FDI) or as investment by Foreign Institutional Investors (FIIs) or Participatory Notes (PNs). As per the existing provisions of Income Tax Act and court rulings, it is not possible to examine the source of source or to reach the tail end of such introduction of unaccounted income. Enquiries into the source in such cases are not possible because there is complex multi-layering or layering is done through entities registered in other countries. Layering transactions to conceal the reality or to hide the ownership should not be permitted and FIIs should not remain faceless entities. In such cases, where there is a suspicion about the genuineness of transactions, there should be provisions in law to treat it as income of the beneficiary unless commercial expediency of the layered transaction is explained. Onus should be on the beneficiary in such cases.

3.13 In case of share application money lying idle for a certain period of time, there should be a provision for taxing the same at some particular rate because the beneficial company is getting capital without paying any interest for that period. Empirical knowledge shows that such kind of capital introduction is generally a method of routing unaccounted money. There is urgent need for legislation so that assessing authorities can go beyond source of the source of such sham transactions, in order to reach the tail end, because due to the certain judicial pronouncements it has become difficult to do so at present. Onus of proving the genuineness of share capital introduction by a company should lie on the company itself. Mere submission of name and address of the share-holders should not absolve them from this onus. The company management should know the identity of the share-holders, and KYC norms should be imposed in the capital market as in the banking sector.

3.14 All tax treaties should have the articles on exchange of information. In cases where we don't have DTAA's, we should go for Tax Information Exchange Agreements (TIEAs). Tax havens which refuse to sign TIEAs with us should be notified as 'non-co-operative jurisdiction' and suitably tackled at international forums. Further, suitable mechanisms should be developed to deal with remittances from/to such tax havens. An effective deterrence could be TDS on such remittances irrespective of their nature if they are coming from a non-co-operative jurisdiction. Only when we have such institutional arrangement for information exchange can we effectively curb the flight of black money. In case of outward foreign remittances exceeding a particular amount, a mechanism should be developed to ensure proper monitoring. For this purpose the TDS mechanism should be geared up. The return form should be amended to make it mandatory for taxpayers to make specific declaration about bank accounts in foreign countries.

3.15 It is a well-known fact that huge amount of black money is re-routed in the books in the form of Long Term Capital Gains arising from share transactions, which is exempt from tax. It is high time that exemption provided in the Act on such transactions is removed. If at all any concession has to be given, then LTCG should at least be taxed at a concessional rate.

### **Non-Profit Sector**

3.16 The definition of “charitable purpose” u/s 2(15) of the Income Tax Act, 1961 is widely being misused by the so called educational societies running the educational institutions on purely commercial basis. Such societies after getting registered under section 11 or 12, or section 10(23C) of the Income Tax Act, 1961 avail 100% exemption from tax, although there is nothing charitable in their activities. Tax scrutiny of such institutions does not yield any worthwhile results. Therefore, there is an urgent need to check proliferation of such education business by making necessary amendments in the definition of charitable purpose u/s 2(15) of the Income Tax Act, 1961. There is an urgent need to amend Sections 2(15) for the definition of ‘Charitable Institution’ with clarity. Section 10(23C), Section 11 and Section 12 also need to be amended so that such institutions do not get blanket permit for generation of unaccounted money. The provision of certain rate of tax or flat rate of tax on gross turnover or profits has been introduced in the Direct Taxes Code Bill. However, respective regulators also have responsibility to ensure discipline in the matter.

### **Tax Free Zones**

3.17 Tax free zones or tax holidays have been created in the various states, viz. Himachal Pradesh and J&K in the North. In some cases, it has been found that the deductions u/s 80IA/80IB of the Income Tax Act being claimed by the Industrial Units are bogus. Mostly Industrial Units allegedly operating from these zones are actually not operating, and if they operate they show higher profits during the years of entitlement for claiming deductions under Income Tax Act, which is not commensurate with trade results in similar lines of business outside such zones. Soon after the tax free period is over, the same business shows sharp drop in returns. From the field experience, it has been established that such zones are merely conduit to channelize unaccounted profits of other regions without paying any tax on the same. Suitable amendments are required in the income tax and other related laws to plug this loop hole. The plethora of exemptions and deductions in the Income Tax Act also need a revisit. The profit linked deductions are prone to misuse as they encourage diversion of income from taxable activities to such activities where deduction from income is available. A beginning has already been made by introducing investment linked deductions in the Direct Taxes Code Bill.

### **Agricultural Income**

3.18 Similarly, the transactions relating to agricultural activities and forest produce are allowed to be done in cash keeping in view the interest of the farmers and the growers. In the garb of these benefits, persons having very little or unproductive land holdings procure false bills from Commission Agents of grains, fruits, vegetables and forest produce, to have exempted agricultural income. Instances have also come to the notice that small farmers having their own agricultural holding of even less than five acres, claim to be doing agricultural activities on land holdings of 50 acres or more under the garb of lease holdings. By doing this exercise, they facilitate the lessor to adjust his black money and also create disproportionate agricultural income in his own hands. So in a way for some piece of agricultural land, both the lessor and the lessee claims the agricultural income quite disproportionately.

3.19 To curb this tendency, the Agricultural Department of every State, who are considered to be the specialist in the field, after making the necessary studies on the yield and market rates, should work out mechanism to notify at least the average yield of the produce of the respective crop for the specific area. This notification should be published at the beginning of every financial year, which can be modified keeping in view other natural factors. Such yield rates should be considered in the case of the assesseees who are showing agricultural income beyond a certain limit of agricultural holdings. Such notification should be legally binding on assessing authorities as well as appellate authorities.



3.20 Many taxpayers use the income tax exemption for agricultural income to bring back tax evaded money into the economic mainstream. While per se this may be productive economically, and agricultural income is also considered for rate purposes while computing income tax liability, ways to tax such amounts, or preventing misuse of these provisions by unscrupulous taxpayers, need to be considered.

### **Corporate Law**

3.21 In India, there are over 6 lakh companies, of which a miniscule number contribute to tax. The remaining companies created are either not profit making or dormant. Such private limited companies use the route of share capital with share premium for the introduction of black money. The modus-operandi is to issue capital with partly convertible shares at huge premium. These investment companies are companies in which cash has been introduced after layering through a number of entities to make detection of the cash source difficult. The premium charged is shorn of commercial reality or basis. After bringing its 'own' capital through partly convertible shares with huge premium, the company usually buys backs all shares at nominal value, thus laundering black money in a prima-facie legal manner.

3.22 Companies with low equity, but having high debtors and creditors without any immovable assets, should be captured in databases, as should be companies which have changed their registered offices frequently in a span of few years. Similarly companies charging premium but not in fact ever allotting shares should create suspicion. The raising of red flags should result in verification and/or investigation of such companies. Ministry of Corporate Affairs should also give serious concern to data mining and intelligence extraction, if companies are to play their due and important role in any growing economy.

3.23 Charging share-premium should be restricted to companies with large paid-up capital – say exceeding Rs.25 crores, and not for small companies where such provision is prone to misuse.

3.24 In many cases, it has been observed that unaccounted income of business groups are brought back into the regular books in the form of share application, share capital and share premium, through bogus investment companies popularly known as 'jama-kharchi' companies. After the decision of the Supreme Court in the case<sup>1</sup> of Lovely Export, taxation of such bogus share capital has become almost impossible. It is imperative to bring necessary amendments in the Act, treating such receipt of share capital and share premium at par with cash credits with onus on the assessee of proving the creditworthiness, genuineness and identity of the share holder. In case of corporate assesses the identity should be deemed to be not established if the directors are not traceable on the address given. Such legislation will go a long way in curbing ploughing back of black money.

### **Expanding Banking Operation**

3.25 With high liquidity and its ramifications for inflation, the re-introduction of BCTT may also be considered. The advantages of re-introduction would be two fold. Firstly, it would discourage cash withdrawals and therefore use of cash, and secondly, large cash transfers could be monitored.

### **Corruption**

3.26 Those holding public office declare their assets before election. There is no requirement (except in income tax returns) to reflect their assets when they demit office. Such a requirement should be mandatory as such information would be accessible under the RTI Act. Politically exposed persons (PEPs), before they take their pension entitlements, could be subjected to scrutiny with respect to accretions in wealth assets.

3.27 The Canadian legislation relating to anti-money laundering law applies to proceeds "obtained or derived directly *or indirectly* as a result of ... an act or omission *anywhere* that, if it had been acquired in Canada would have constituted" an offence under Canadian law. This aspect needs to be incorporated

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<sup>1</sup> CIT vs. Lovely Exports (P) Ltd. (2008) 6 DTR 308 (SC)

in the Indian law through Prevention of Money Laundering Act (PMLA) – so that illegal proceeds generated not only domestically but also internationally are covered. Such illicit flow of funds to the developed countries from the developing countries can be substantially reduced.

### **Introducing Beneficial Ownership Concept**

3.28 The concept of beneficial ownership as introduced in the PMLA may also be incorporated in the Income Tax Act while dealing with the provisions of bogus share capital. It is defined as under

“beneficial owner shall mean the natural person who ultimately owns or controls a client and/or the persons on whose behalf a transaction is being conducted, and includes a person who exercises ultimate effective control over a juridical person”

### **Fund Transfers Abroad**

3.29 There must be a specific column in the return of income asking the assessee to state whether he holds any off-shore bank account or assets and if so, there should be a reporting requirement of the details thereof. Necessary amendments in the Income Tax Rules and the Income Tax Return Forms may be made. This must be accompanied by specific harsh penal provisions and prosecution under criminal law for furnishing incorrect information. This would act as a deterrent to assessees who hold undisclosed off shore accounts/assets.

3.30 It is also known that money stashed abroad is generally kept in certain overseas branches of foreign banks who refuse to give information even after being provided with full-fledged information of such bank accounts. Enforcement agencies in India should be empowered to issue subpoena to the Indian Branches to cull out the information available in consultation with RBI with its foreign counterpart. The RBI may frame rules wherein the Indian Branch is given a business disincentive as the closure of business if the said information is not provided by the Indian Branch.

3.31 It is also suggested that in some of the DTAA's where there is much emphasis on Secrecy Clause, the treaties may be renegotiated on the lines of OECD Model Tax Convention Article 26. A new Clause should be inserted in the treaties by signing Protocols prohibiting the country from withholding of information on the ground/ pretext that the said information is not needed by their Tax Departments or their domestic law prevents the FIs or banks to pass on such information. If such an amendment is brought then the contracting countries will not have any ground to refuse information. This practice is now being adopted by all the developed countries and tax havens are being pressurised to give information.

### **Foreign Remittances**

3.32 Over-invoicing and under-invoicing of imports and exports is a regular phenomena, and the difference in prices of goods and services are settled through Hawala route or by adjustments. While the transfer pricing regulations check such transactions between associated enterprises, they have no role in cases of transactions between unrelated transacting entities. Therefore, stricter laws need to be implemented so that such operators should be punished expeditiously.

3.33 Use of the Mauritius route and other tax havens, as channel for avoiding payment of taxes in India, with the help of loopholes in bilateral agreements on double taxation, may be stopped by bringing in appropriate legislative changes either in the Act or in the respective DTAA's. Suggestions to strengthen the laws could be the following:

- (a) Withdraw or amend Circulars No. 682 and 789 issued by the CBDT.
- (b) Make round tripping clause in the DTAA's with stringent non applicability of treaty benefits, or necessary changes be brought in the law.
- (c) Strengthen the laws for monitoring of investments in/from India into a zero/low tax countries.

3.34 Replacement of laws treating economic crime as criminal offence instead of civil offence under FEMA. There is room for thought to consider whether some concept of criminality *mens rea* under FEMA has to be brought back especially in repetitive offences, offences involving securities markets, etc.

3.35 Share market is one of the sectors where ill-gotten money sourced abroad is brought back through transactions from tax havens or low tax jurisdictions. Unfortunately, the KYC norms are not fully and really extended to the FIIs, their sub-accounts, their Participatory Notes ('PNs') and other non-resident investors. Presently, the mere fact that they are registered with some Regulatory authority in any country shields them from the further investigations by the Indian agency. This soft glove treatment should be stopped and SEBI as well as Income Tax Department and Enforcement Directorate should be empowered to ask for the actual identification of these investors' sub-accounts and PNs etc.

### **Law & Procedures**

3.36 The Law Commission should be entrusted to suggest ways, including legal enactments, which could provide for harmonizing various proceedings under different financial laws. This would include procedures to formalise setting up teams, where investigation officers from different departments, even ministries, could be formed for any enquiry. The main and basic offence should determine the nodal Ministry/Department to provide the team leader, who in turn would have members of the team from all other departments/ministries till such investigation is complete. This is a practice followed in the U.S., which too has a federal structure, but has an effective, workable system, without which there can be no effective deterrence.

3.37 Under Section 131 of the Income Tax Act, there is a requirement of nexus between the documents called for and the proceedings pending, and the I-T authorities cannot make roving enquiries. Action for false statement under oath cannot be taken under IPC. Under the CPC, a warrant of arrest may be obtained for production of the witness to the court or else prosecution proceedings can be initiated under section 174 of the IPC for failure to respond to summons. Failure to comply to a summons can also entail a search under section 132 of the Income Tax Act. However, launching prosecution is a cumbersome process. As time is of great essence in investigation of a tax evasion case, it is not possible to conduct a search in every case of non-compliance. Section 272A(1)(c) of the Income Tax Act prescribes a penalty for non-compliance to summons under section 131 of Rs. 10,000 for each such default which is hardly a deterrent. Therefore, provisions akin to CPC/IPC need to be incorporated in the income tax law to enforce attendance of witnesses. The quantum of penalty imposable under section 272A(1)(c) also needs to be enhanced to have effective deterrence.

3.38 At present, Income tax authority is empowered to carry out survey u/s 133A of the Income Tax Act only in a premise at which a business or profession is carried on. Therefore, an institution or trust, apparently having charitable object, cannot be covered under section 133A. However, in many cases, charitable institutions are being run on commercial lines for generating profits, though the declared objectives of the institutions are stated to be charitable in nature. This impediment should be removed.

3.39 There is no power to call for witness during survey, if the assessee is uncooperative. The words 'on oath' should be inserted after the words 'record the statement of any person' in the wording of Section 133A (3)(iii) so as to preclude the possibility of retraction at a later stage. Provisions on the lines of Section 132(4A) should also be introduced in Section 133A, so as to create presumption of ownership as regards books of accounts, etc., found in the course of survey.

3.40 No power is vested in Directors of Income Tax (Investigation) to grant sanction for prosecution for offences that occur in connection with the work area related to the Investigation Directorate i.e. under sections 275A, 275B, 277A and 278 of the Income Tax Act, 1961. This should be introduced in the Income Tax Act.

3.41 Penalties that are not related to assessment, such as for failure to maintain books/get accounts audited, etc., the penalty amount is too low to act as an effective deterrent. For instance, penalty under section 271A for failure to keep, maintain or retain books of account, documents, etc. is ₹25,000 which will hardly act as an effective deterrent.

3.42 There is no provision under the income tax law to determine whether any income/asset are from legal or illegal means. This should be introduced in the law and stringent taxes and penalties imposed for illegal income/wealth. Maximum marginal rate can be enhanced for charging undisclosed incomes.

3.43 Though there are rules for arriving at arm's length price (ALP) in the case of international transactions with related entities, there are no such rules for arriving at ALP in transactions with unrelated entities whether within the country or outside, which should also be considered.

3.44 There is no power of contempt or grant of summary punishment for false evidence, or enforcing attendance of witnesses or committing a person to give evidence or produce books/documents. For effective criminal investigation against tax evaders, provisions akin to Chapter-XXVI of Cr PC need to be introduced in the Income Tax law.

3.45 The Forms No. 60/61 and Form 15G/15H should be suitably modified so as to also capture the fields such as "Date of Birth", "Date of Incorporation" and "Father's Name" for population of valid PAN in non-PAN data collected by CIB units. Obtaining copy of KYC documents should be made mandatory.

## **DIRECTORATE OF REVENUE INTELLIGENCE**

4.1 For execution of the provisions of forfeiture of properties under the customs and narcotics laws, the difficulties faced are mainly identifying the property, identification of relatives/associates in whose name the property is acquired, lack of co-ordination between different agencies, shortage of resources/manpower, paucity of time, etc. Until all revenue records indicating the ownership of any property are computerized/connected all over India through a server, it is an tedious job to identify property owned by an offender particularly when it is at a place, other than the city of his residence.

### **4.2 Bilateral agreements or the International Convention on Mutual Administrative Assistance for the Prevention and Repression of Customs offences (CMAAs)**

The role of international cooperation in effective Customs enforcement can hardly be over emphasized. India has signed bilateral cooperation agreements/ Memoranda of Understandings with 20 countries (which include EU and SAARC Blocks). This arrangement helps the Customs Department in gathering information and investigative assistance relating to Customs offences which have direct linkages with the generation of black money. Although the experience, so far, in this regard has generally been positive, successful partnership depends on interest and the willingness of the partner country and also their domestic privacy laws and other legal provisions. However, the world over there is an increasing desire for mutual cooperation and sharing of information. CMAAs are very effective in checking invoice manipulation and other trade malpractices. Strengthening and expansion of CMAAs will be highly beneficial to the cause of curbing the menace of black money generation and its movement across international Borders. It would be useful if the scope of such agreements is expanded and such agreements are concluded with a larger number of countries. India has also made a proposal in the W.T.O. at Geneva for a multilateral agreement for such exchange of information.

4.3 The Central Government has provided for schemes envisaging incentive in respect of Central Excise duty to units located in North East States, H.P, Uttarakhand and J&K. This scheme is being operated by way of exemption from central excise duty to units manufacturing goods in H.P and Uttarakhand. However, in the case of North East and J&K, this scheme is being operated by way of refund of central excise duty paid in cash on finished goods. The refund scheme provides double benefit in view of the fact that the buyer of the goods gets CENVAT credit also and further it is prone to misuse in the following manner:

- a) Over production is shown in order to get more refund of excise duty and clandestinely removed goods, on which no central excise duties have been paid, are regularized and find their way into the mainstream without payment of any taxes and at the same time input credit is availed using invoices of units located in these States.

- b) In most of the cases inputs are shown procured from traders to avoid credit of the CENVAT to maximize the refund and this modus operandi also facilitates diversion of inputs to other units located in tax zones ( particularly to SSI units).

Accordingly, it is proposed that exemption from Central excise duty may be provided to units located in J&K and the North East (similar to H.P and Uttarakhand) and refund scheme may be done away with.

4.4 A detailed 'Risk Management System' (RMS) has been put in place to facilitate the import clearance of reputed clients and low risk consignments. In the face of ever increasing global trade and growing volume of import cargo, RMS ensures better utilization of existing resources to deal more effectively with suspected/targeted cases of misdeclaration and non-compliance. Regular examination of medium and high risk consignments is done to rule out misdeclaration. Moreover, there are various enforcement agencies at different levels to detect cases of misdeclaration. Every year, thousands of cases of undervaluation and misdeclaration are detected at different levels and the importers are appropriately penalized and are made to pay the correct amount of import duties along with interest if any. Search, summons, seizure and arrest provisions have been provided in the Customs Act, 1962 to deal with cases of undervaluation and misdeclaration as criminal offences. Depending on the magnitude of the case, penal provisions including imprisonment already exist in the Act *ibid*. However, Hon'ble Supreme Court in September, 2011 has declared that offences under the Customs Act are non-cognizable and bailable, which is posing legal problems in investigation of the cases by Customs Preventive formations including DRI. A suitable amendment may be carried out in the provisions of the Customs Act to declare the offences under the Customs Act as cognizable and offences under section 135 of the said Act may be made non- bailable.

4.5 In some cases, it has been noticed that foreign remittances against exports are received from third parties who are other than the consignees and are not related to either buyer or consignees. This provides for a mechanism where goods are consigned to and cleared at a place at some declared value whereas highly inflated payments for the said transaction is routed through another entity situated somewhere else. The use of this mechanism facilitates the illegal cycle of flow of funds for the purpose of export benefits only. Accordingly, the banking system should be advised to curb the misuse of banking provisions by employment of the aforesaid modus operandi. Proper verification of foreign remittances may be done by banks and bank realization certificates for realization of export proceeds may be issued only thereafter in cases of remittance received from third parties. This will help in curbing the illegal inflow of black money as well as the burden on the exchequer on account of undue export incentives.

4.6 Section 142 of the Customs Act, 1962 provides for recovery of dues from sale of goods under Customs control or movable/immovable property of the person from whom the amount is to be recovered. However, it does not provide for recovery of sale proceeds of smuggled goods. The section should be amended to provide for recovery of sale proceeds of smuggled goods i.e black money generated/ transferred in international trade.

4.7 Section 28BA of the Customs Act, 1962 provides for provisional attachment of properties where show-cause notice (SCN) has been issued u/s 28(1). However, it does not provide for such provisional attachment in cases of SCN issued u/s 28 (4) or other circumstances like drawback fraud. The section should be amended to provide for provisional attachment of property in respect of SCN issued u/s 28(4) and in other cases such as duty drawback fraud to protect the interest of revenue.

4.8 Existing provision under the Customs Act, 1962 provides for punishment by way of imprisonment up to 7 years for smuggling of FICN. However, the very nature of this illegal activity makes it highly dangerous to any economy in particular and to the world trade in general. Stringent laws, including enhancing the length of punishment from 7 years under the existing laws, should be incorporated to deal with FICN more effectively.

## **DIRECTORATE OF CURRENCY**

5.1 The Government had constituted two Committees for suggesting reforms in those two areas, which are more prone to corruption and generate a significant amount of black money. Both the Committees have already submitted their reports to the Government and this committee suggests that decisions must be taken urgently in a time bound manner to plug the known source of generation in black money. The Reports are summarised as under:

### **A. REPORT OF THE COMMITTEE ON PUBLIC PROCUREMENT:**

A.1 Corruption in public procurement and contracting is an important source of generating black money. The government and its agencies incur huge amount of public funds on the procurement of goods and services for various welfare programmes and also for their own use. It is fact that the public procurement is a necessary and all pervasive activity within Government and its organisations, stretching across the breadth and depth of the Government structure. However, efficiency and probity in public procurement, on the one hand, determines the efficacy of the utilization of public funds and on the other hand, it affects the public perception of the credibility of public procurement in particular and the level of governance in general.

A.2 The view has long been held that there is need to undertake systemic and procedural improvements in this area. The recent revelations of mal-practices in high profile procurements have only brought out the urgency of need to reform in this area. Therefore, the Government had constituted a Committee on Public Procurement under the Chairmanship of Shri Vinod Dhall to suggest a comprehensive procurement policy to reform public procurement. The Committee looked into various issues having an impact on public procurement policy, standards and procedures.

A.3 The recommendations of the Vinod Dhall Committee are aimed at bringing efficiency, transparency and accountability in the public procurement. The Committee has proposed basic reforms in the whole area of public procurement, including the legal and regulatory framework, the institutional structure, the deployment of modern technology in aid of public procurement, as well as overhaul of certain specific prevailing practices. The emphasis is on transparency and putting maximum information in public domain i.e., public procurement legislation and an overarching e-portal (public procurement portal) that acts as a one-stop shop for tendering, bidding and payments of earnest money.

A.4 The last CoS meeting on this subject was held on 8.8.2011. It was observed in this meeting that a statement laying down the over-arching policy on procurement may be issued and work on drafting a law may be taken up. Department of Economic Affairs had also agreed to go for a separate law on public procurement. Accordingly Department of Expenditure vide their OM No. 2/3/2011-PPC dated 2nd December 2011 have circulated the Draft Public Procurement Bill for inter-ministerial consultations. It is therefore necessary that steps are taken in a time bound manner to help in bringing to an end this important source of generating black money.

### **B. COMMITTEE ON ALLOCATION OF NATURAL RESOURCES:**

B.1 Another significant source of generating black money is the alleged discretionary and non-transparent allocation of natural resources. Therefore, a Committee on Allocation of Natural Resources (CANR) was constituted by the Government under the chairmanship of Mr. Ashok Chawla, former Finance Secretary, inter-alia to deliberate on issues of enhancing transparency, effectiveness and sustainability in utilization of natural resources, consistent with the needs of the country to achieve accelerated economic development.

B.2 The committee identified natural resources such as coal, minerals, petroleum, natural gas, spectrum, forests, water and land, wherein the Union Government had a major role to play in articulating the policy framework or otherwise influencing the manner of their allocation. The important recommendations of the CANR relate to, among other things, standardising the format of minutes for all

Standing Linkage Committee (Long-Term) meetings, particularly for meetings where allocation decisions are made. It has also proposed that Mines and Minerals (Development and Regulation) [MMDR] Bill, 2011 which has been drafted to replace the existing MMDR Act, 1957 may accommodate a variety of allocation mechanisms – both for areas of known and unknown mineralization – provided they are open, transparent and competitive.

B.2 The committee mainly recommended that the Government should put in place transparent market-based mechanisms in the allocation and utilisation of natural resources. The Committee has also recommended that while it is important for market processes to be used wherever relevant and feasible, the capacity for oversight is an integral component of an institutional architecture that ensures transparent, efficient and sustainable allocation and use of natural resources.

B.3 The GoM in its sixth meeting dated 30th September 2011 considered the recommendations of COS dated 29th September 2011. After detailed deliberations, most of the recommendations of the CANR were accepted as proposed by the Committee. DEA was asked to prepare a policy paper with regard to transfer or alienation of land held by Government and Government controlled statutory authorities, and take further necessary steps to bring it to the Cabinet for final approval urgently. These steps shall ensure monitoring over leakages from the system in form of black money and will also bring more revenue to the Government.

5.2 Ratification of Palermo Convention: The ratification of Palermo Convention will help in getting cooperation from foreign jurisdiction on the basis of this multi-lateral treaty (i.e. Palermo), in those cases wherein India doesn't not have Mutual Legal Assistance Treaty on criminal matters. The scope of cooperation shall include both of collection of evidence and causing confiscation of assets linked to Scheduled Offence in India.

5.3 Implementation of recommendations of Committee on Beneficial Ownership. This will help in identifying the beneficial owners of the legal entities.

5.4 Signing of MOU by RBI with Chinese Banks, and others, will open another channel of accessing information of a customer of foreign bank, which is of interest to India.

5.5 Directorate of Currency needs to overcome the issue of counterfeiting and ensure that coins and currencies are machine readable, which will make the routing of cash transactions through banks more easy, user-friendly and attractive. The DoC needs to be strengthened to achieve these objectives. This will go a long way in eliminating cash transactions, which are conduit for black money.

### **FINANCIAL INTELLIGENCE UNIT (FIU-IND)**

6.1 The issue of black money is complex and has many facets that must be analyzed before adopting a prescriptive approach. There should be a commonly agreed definition, the causative factors, the modus operandi for generation, concealment and transaction of black money, in order to evolve a comprehensive and integrated regime to combat black money. Subject to this, some general suggestions that could help mitigate the problem of black money are as follows:

A. Equal focus on black money in India and that in foreign countries:

6.2 A lot of attention has recently been given to black money transferred abroad. Any policy on recovery of black money should give equal, if not more, importance to the fact that large amounts of black money are circulating within the country. The recovery of the domestic component of black money is relatively easier compared to retrieval of black money stashed in foreign jurisdictions, which requires co-operation from other sovereign countries having their own legal system and procedures. Effective handling of the issue domestically can produce tangible results with comparatively less efforts and resources.

B. Effective mechanism to track benami assets:

6.3 The Benami Transactions Prohibition Act has not yet come to force despite having been passed

in 1988. In view of the fact that benami assets are an important means of investing black money, the operationalization of the Act should be facilitated, with appropriate changes, if necessary, to make it relevant under the current socio-economic situation.

C. Effective mechanism to track and confiscate proceeds of crime:

6.4 The effectiveness of the existing legal and executive framework to detect and confiscate incomes and assets of criminal origin should be reviewed and enhanced. Speedier investigation and prosecution to effect confiscation and forfeiture of proceeds of crime appear feasible in view of the fact that under PMLA, the burden of proving that the proceeds of crime are untainted property is on the accused.

D. Tax-related offences as predicate to money laundering:

6.5 An international debate is underway on the desirability and feasibility of making tax offences as predicate offences under the anti-money laundering legislation. Certain countries like the United Kingdom and Germany already treat tax offences as predicate offences under their anti-money laundering legislations. India could consider aligning its policies on this issue with the standards that would emerge from the deliberations of the Financial Action Task Force (FATF).

E. Reporting of foreign remittances:

6.6 Foreign remittances using corporate structures and the formal financial sector infrastructure could possibly be a popular method of transferring funds (even of illegal origin) to foreign jurisdictions or even for routing back to India through Foreign Institutional Investment (FII). There is a need to create a robust database of such remittances and carry out an analysis of their backward and forward linkages in order to understand the nature and legitimacy of the funds transmitted. FIU-IND may be empowered by law to receive reports (similar to other reports submitted to FIU-IND) on all international funds transfers through the Indian financial system. The FIUs of Australia and the USA are already mandated to receive such reports.

F. Database of new and closed bank accounts:

6.7 There is also a need to have a central database of all accounts opened and closed in all financial institutions in the country. This database would be of immense help in identifying all the accounts that a person suspected of having black money is operating all over the country, including accounts of his close relatives and business concerns.

6.8 The Financial Intelligence Units (FIU) all over the world are essentially the creation of FATF Recommendations. In the Egmont Group (an organization of all FIUs in the world) the Indian FIU has gained eminence due to its technical and other expertise, and FIU-IND has also come in for exceptional praise by the onsite FATF team. An essential criterion for compliance to FATF Recommendation is autonomy in FIU's organizational structure and its functioning as required by the FATF. Therefore, the FIU should not be kept under the administrative control of the Government for its core functioning, which is collection, analyses and dissemination of financial intelligence.

6.9 The Central Economic Intelligence Bureau (CEIB), which is already collecting data from state police on fake Indian currency notes (FICN), may utilize the resources of FIU by sharing complete details of FIRs filed by the state police, which would act as the data base for the FIU and in turn make the anti money laundering and CFT regime stronger. For this purpose CEIB may consider having an MOU with FIU, on the lines of CBI's MOU with FIU.

## **DIRECTORATE OF ENFORCEMENT**

7. Comprehensive amendments to the PMLA have been recommended by the Directorate of Enforcement to the Department of Revenue to make the anti-money laundering law more effective. These are at an advanced stage of consideration.



## **TRADE/INDUSTRY BODIES**

8. The response of trade & industry bodies to the request for suggestions has not been very encouraging. Only FICCI and ASSOCHAM responded. Their suggestions include bringing transparency through use of technology, reducing the informal and cash economy, prohibiting personal expenses in cash by certain limits, implementing the GST regime, and bringing a scheme to declare undisclosed assets.

## **SUGGESTIONS FROM PUBLIC**

9.1 One common demand from the public is that high denomination currency notes, particularly ₹1,000 and ₹500, should be demonetized. In this connection, it is observed that demonetization may not be a solution for tackling black money or economy, which is largely held in the form benami properties, bullion and jewellery, etc. Further, demonetization will only increase the cost, as more currency notes may have to be printed for disbursing the same amount. It may also have an adverse impact on the banking system, mainly logistic issues, i.e. handling and cash transportation may become difficult and may also cause inconvenience to the general public as the disbursal or payments of wages/salaries to the workers will become difficult. Besides, it may also adversely impact the environment as more natural resources would be depleted for printing more currency notes. Demonetization undertaken twice in the past (1946 and 1978) miserably failed, with less than 15% of high currency notes being exchanged while more than 85% of the currency notes never surfaced as the owners suspected penal action by the government agencies.<sup>2</sup>

9.2 Some other recommendations received from the public, inter alia, are:-

- (i) Declaring black money as national asset and confiscating illicit wealth;
- (ii) More stringent laws and punishments, including life-term for those indulging in corruption or stashing black money abroad;
- (iii) Special courts should speedily try cases of corruption and economic offences;
- (iv) Expand banking operations and use of modern net-driven/mobile technology in monetary transactions;
- (v) More transparency in government functioning, particularly in tendering, award of contracts, payments, and delivery of services ;
- (vi) Reduce taxes, such as stamp duty, capital gains tax, etc., and simplify procedures;
- (vii) Increase public awareness about ills of black money and corruption by including it in school curriculum, launching public campaigns, publishing names of tax-defaulters and persons with illicit accounts abroad;
- (viii) Bring a voluntary disclosure scheme with/without penalty and then strictly enforce economic laws;
- (ix) Reward to informants of black-money;
- (x) Increase the effectiveness of departments dealing with tax laws – increase their manpower, ensure its integrity, incentivize them with 1% of the black money detected, develop good intelligence;
- (xi) Bring strong Lokpal Bill to monitor and punish political corruption, dismissal of public servants found to indulge in corruption, debar corrupt politicians from contesting elections; etc.

## **MEASURES FOR UNEARTHING BLACK MONEY**

### **Provisions to get information, confiscation of foreign assets, etc.**

10.1 Different agencies of the Government are engaged in collection of information, which can be

<sup>2</sup> NIPFP & Gupta reports, op cited

used in identification of black money. The Central Board of Direct Taxes (CBDT) and Central Board of Excise & Customs (CBEC) are apex tax bodies of the Central Government and mainly tasked to check the evasion of taxes and trade-based generation of black money. Reporting mechanisms are prescribed under the laws governing levy of income tax, customs, excise and service tax; FEMA and NDPS Act, etc. Financial institutions and intermediaries registered with SEBI are required to furnish details of transactions to the income-tax authorities. Besides, other ministries /departments, such as Ministry of Corporate Affairs, Ministry of Commerce & Industry, and various agencies under them also collect information of varied kinds. Information is sometimes also exchanged in terms of proceedings for bilateral agreements for civil and criminal court proceedings on a case to case basis. Under the EGMONT<sup>3</sup> set-up, Financial Intelligence Units (FIUs) of various countries, including FIU-INDIA, also exchange information. The information exchanged by FIUs may pertain to a whole range of predicate offences and the associated money laundering as well as terrorist financing and can be used by the recipient authorities, subject to prior authorisation of the authority that provided the information. However, the most comprehensive provisions for the exchange of outside information exist in the double tax avoidance or tax information exchange agreements/treaties that India has with various countries (details given later).

10.2 India has criminalised money laundering (ML) under both the Prevention of Money Laundering Act, 2002 (PMLA) as amended in 2005 and 2009, and the Narcotic Drugs and Psychotropic Substances Act, 1985 (NDPS Act), as amended in 2001. India's anti-money laundering regime is centred on the PMLA with the formal objective to prevent money laundering and to provide for confiscation of property derived from or involved in money laundering. Section 3 of the PMLA provides that the offence of money laundering is committed where someone "directly or indirectly attempts to indulge, knowingly assists or knowingly is a party or is actually involved in any process or activity connected with the proceeds of crime and projecting it as untainted property". The Unlawful Activities (Prevention) Act, 1967 (UAPA) tackles the matters relating to terrorism and its financing. The UAPA was amended in 2004 and 2008 to criminalise, inter alia, terrorist financing and to strengthen the fight against terrorism and terrorist financing.

10.3 Counterfeit currency is also one of the sources of generating black money in the country. Therefore, the Directorate of Currency (DoC) has been created in the Ministry of Finance with the approval of the Cabinet. The DoC, inter-alia, monitors and reviews the efficacy of the existing security features in the currency notes. The Directorate of Currency has initiated the process to further upgrade the security features to be incorporated in new series of bank notes expected to be issued in 2012.

10.4 India has committed various issues to FATF through Action Plan, which would help in creating adverse climate to money laundering. The assets of criminals acquired through laundering either in the country or abroad shall be targeted in a greater strength. Amongst the committed issues, some of them having more direct bearing on detection of black money (crime money) are as under:

- (i) Section 3 of PMLA criminalize the act of laundering of proceeds of crime relates to Scheduled Offences (i.e. listed offences). The offences listed in Part- B of Schedule can be presently investigated only if proceeds of crime are to the tune of Rs.30 lakhs or more. This threshold is likely to be removed in the proposed amendments. As a result, larger number of fresh cases would be available for investigation under the Act.
- (ii) The procedure for confiscation of proceeds of crime has been provided in Section 8. The existing procedure is very lengthy, cumbersome and linked with the conviction in predicate offence. The said procedure is being simplified in the proposed amendment, which shall help in expediting of confiscation action.

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<sup>3</sup> Recognizing the benefits inherent in the development of a network, in 1995 a group of Financial Intelligence Units (FIUs) met at the Egmont Arenberg Palace in Brussels and decided to establish an informal group whose goal would be to facilitate international cooperation. Now known as the Egmont Group, these FIUs meet regularly to find ways to cooperate, especially in the areas of information exchange, training and the sharing of expertise.

- (iii) The FIU-IND is presently generating large number of STR's which are being used by Income Tax department for detection of concealed/undeclared transactions by reported persons/entities. It is expected that in coming years, FIU-IND would may significant role in tracking such transactions and thus help reduce black money in the financial system.

#### Five-pronged strategy of the Government<sup>4</sup>

In order to unearth black money kept abroad, it is necessary that there is (i) information about the money kept abroad, (ii) adequate legislative and administrative framework to deal with the problem, and (iii) perhaps an enabling scheme for offshore compliance to help inadvertent tax-evaders comply with their tax obligations.

11.1 The Central Government has formulated a five pronged strategy<sup>5</sup> for taking action as regards black money kept abroad. The strategy adopted is as follows:

- (i) Joining the global crusade against '*black money*';
- (ii) Creating an appropriate legislative framework;
- (iii) Setting up institutions for dealing with illicit funds;
- (iv) Developing systems for implementation; and
- (v) Imparting skills to the manpower for effective action.

11.2 In line with above strategy, the Government has taken several steps in the last two financial years. India as a member of G20 has played very active role in raising various issues relating to curbing the menace of black money, viz. financial transparency and end to banking secrecy (April 2009 at London Summit); develop toolbox of counter measures against non-cooperative jurisdictions (September 2009, Pittsburgh); declaration to conclude Tax Information Exchange Agreement (Seoul Summit, November 2010); getting past banking information (Paris, February 2011 & Washington, April 2011).

11.3 Global Forum on Transparency and Exchange of Information for Tax Purposes was reconstituted in 2009. India has played a key role in finalizing the terms of reference, methodology, assessment criteria and schedule of reviews at New Delhi in February 2010. In June 2010 India became the 34th member of Financial Action Task Force, responsible for enforcement of anti-money laundering (AML) and combating financing of terrorism (CFT) regime. India joined the Task Force on Financial Integrity and Economic Development in order to bring greater transparency and accountability in the financial system. India gained membership of the Eurasian Group (EAG) in December 2010, and is actively participating in policy groups of OECD and UN on Exchange of Information, International Taxation and Transfer Pricing as observer and member respectively. India has also recently signed the Convention on Mutual Administrative Assistance in Tax Matters as amended by the 2010 Protocol.

11.4 In 2009 India had 78 Double Taxation Avoidance Agreements (DTAAs) in force (**TABLE-E1**). Out of these only 3 countries namely Iceland, Tajikistan and Myanmar already had specific provisions for exchange of information. Although in the balance 75 treaties, there are Articles on "Exchange of Information", in a number of cases, they are not as per current International Standards. Accordingly, steps are being taken to bring them to the International standards. Simultaneously, negotiations with some other countries (apart from the 78 countries with whom DTAAs existed in 2009) have also been initiated. While negotiating new DTAAs, the Government has ensured that the Article concerning exchange of information is in accordance with international standard. Significant progress has been made by India in this regard during the past two years. As on date, negotiations have been completed with **28** countries with which India already has **existing DTAAs**. These agreements have also been initialled by the respective countries. **19** new DTAAs have also been **finalised**, where the Exchange of Information Article is in line with international standards. Thus, **negotiations/re negotiations** of DTAAs with **47 countries** have been

<sup>4</sup> Inputs from FT&TR Division of CBDT

<sup>5</sup> Announced by Finance Minister in the Press Conference on 25<sup>th</sup> January, 2012

completed, out of which 15 DTAAAs have been finally signed. The current status of negotiations is summarized at **TABLE-E2**.

11.5 The amendment to tax treaty with **Switzerland** has also been signed and approved by the Parliament of Switzerland on 17th June 2011. It has entered into force on 7th October 2011. The amended Protocol will allow India to obtain from Switzerland, in specific cases, banking information (as well as information without domestic interest) which relates to period starting from **1st April 2011**.

11.6 India is trying to include in its DTAAAs an Article relating to Assistance in Collection of Taxes. Only 30 DTAAAs contain an Article on Assistance in Tax Collection. Most of the countries do not wish to have this article as it involves commitment of domestic resources for collection of tax demand of the other country. With certain low tax jurisdictions, India has taken steps to sign Tax Information Exchange Agreements (TIEAs) in place of comprehensive DTAAAs. The current status of these requests is summarized at **TABLE-E3**. In all the TIEAs negotiated by India, there is provision for Tax Examination Abroad which will help the Government in sending its officers abroad for investigation. Government has also enacted legislation to prescribe tool box of counter measures as an anti-avoidance measure by inserting section 94A into the Income-tax Act through Finance Act, 2011.

11.7 The following specific new provisions are proposed for checking generation of black money in the **Direct Taxes Code Bill**:

- a. For the purpose of levy of wealth tax, taxable assets have been defined to include deposits in banks located outside India in case of individual, unreported bank deposits in case of others, interest in a foreign trust or any other entity (other than foreign company) and any equity or preferential shares held in a controlled foreign company.
- b. The General Anti Avoidance Rule (**GAAR**) has been incorporated to deal with aggressive tax planning devices used to circumvent tax laws.
- c. Specific Controlled Foreign Company (**CFC**) rules have been incorporated to bring to tax passive income earned by residents from substantial shareholding in companies situated in low tax jurisdictions.
- d. A reporting requirement has been introduced making it obligatory on the part of resident assesseees to furnish details of their investment and interest in any entity outside India in the form and manner as may be prescribed.

11.8 The Prevention of Money Laundering Act (**PMLA**) was amended on 1st June 2009, whereby the predicate offences listed in the Schedule of the Act were substantially increased. This amendment has widened the scope of money laundering investigations.

11.9 Government has set up dedicated computerised Exchange of Information (**Eol**) Cell for an effective exchange of information to curb tax evasion and also created the **Directorate of Income Tax (Criminal Investigation)**, or **DCI**, in the Central Board of Direct Taxes vide a notification dated 30th May 2011. The DCI, headed by a Director General of Income Tax (Criminal Investigation) at New Delhi, will perform functions in respect of criminal matters having any financial implication punishable as an offence under any direct tax law. The Government has already set up Income-tax Overseas Units in two Indian Missions abroad, and eight more such units are being setup to strengthen the information exchange mechanism. The Government has strengthened the Foreign Tax Division, which deals with the work of exchange of information, and the Investigation Division of CBDT. The Directorate of International Taxation and Transfer Pricing in the Income-tax Department have been strengthened, as flow of money outside India also takes place through mispricing of international transactions. The Directorate of Enforcement has also been strengthened by creating additional posts. As a part of capacity building and skill development, 80 officers were imparted specialized training in the field of International Taxation and Transfer Pricing in the last two years. Foreign training for officers in investigation and criminal investigation matters is also in the pipeline.

## Results achieved

11.10 The fight against black money, both inside and outside the country, has yielded the following results in the last few years:

- I. On the basis of information received from German tax authorities, tax assessments were completed in 18 cases resulting in detection of undisclosed income of Rs.39.66 crore and tax demand of Rs.24.26 crore, out of which Rs.11.75 crore has already been recovered. Prosecution complaints have been filed in 17 cases for various offences under the Income-tax Act, 1961.
- II. 9,920 pieces of Information regarding details of assets held and payments received by Indian citizens in several countries have been obtained which are under different stages of investigation.
- III. On the basis of investigations into information received from France, in 219 cases, undisclosed income of Rs.565 crore has been detected and taxes amounting to Rs.181 crore have already been realized so far.
- IV. Specific requests for information have been made to various countries in 350 cases by tax authorities till date.
- V. 38,828 pieces of domestic information about suspicious transactions has been obtained by FIU which are under investigation by respective agencies.
- VI. Investigation wing of CBDT has detected concealed income of Rs.18,750 crore in last two financial years (FY 2009-10 & 2010-11). During the first ten months of the current year, concealed income of Rs.3,887 crores have been detected. Focused searches have been conducted in a number of cases in the current year on the basis of information received from foreign jurisdictions as also domestic sources.
- VII. Directorate of Transfer Pricing has detected mispricing of Rs.66,085 crore since 1.4.2010, preventing shifting of equivalent profit out of the country. Directorate of International Taxation has collected taxes of Rs.33,784 crore from cross broader transactions in last two financial years.
- VIII. International organisations like Global Forum, OECD, Task Force on Financial Integrity, etc. have appreciated the role that India is playing in the crusade against black money.

## Amendments to the Income Law<sup>6</sup>

12.1 Section 90 of the Income-tax Act may be amended retrospectively to define the meaning of the term “may be taxed”, used in various DTAAs/DTACs, in order to protect the interest of revenue.

12.2 Section 118 of the Direct Tax Code Bill, 2010 provides that the Central Board of Direct Taxes, with the approval of the Central Government, may enter into an advance pricing agreement (APA) with any person. Similar provision may be introduced in the Income-tax Act, 1961 so that APA regime can be implemented from 1.4.2012.

12.3 GAAR and CFC provisions are included in the Direct Tax Code Bill 2010. Similar provision may be introduced in the Income-tax Act, 1961 so that these provisions can be implemented from 1.4.2012. Further, an amendment may be made so that GAAR, CFC and specific anti-avoidance measures in the Income-tax Act, override the agreements entered with foreign countries or specified territories or specified associations, under section 90 or 90A of the Act.

<sup>6</sup> Suggested by FT&TR Division of CBDT

12.4 In recent times it has been observed that when information is received in respect of undisclosed assets held abroad, the Assessing Officer is not able to bring such income to tax because of the time limitation imposed by the Income Tax Act. At present, section 148 read with section 149 of the Act imposes a time limitation beyond which past assessments cannot be re-opened to bring to tax such income which has escaped assessment and is represented by undisclosed assets held abroad. This time limitation has been prescribed for the sake of bringing certainty in tax assessments but is presently emerging as a major bottleneck in bringing to tax income represented by undisclosed assets held abroad. Necessary amendments in the Act should be made to ensure that whenever such undisclosed income represented by assets held abroad is detected, it is brought to tax irrespective of the period to which such undisclosed income pertains.

12.5 To facilitate Exchange of Information, a new clause (viii) has been inserted in Explanation to Section 153 in the Income Tax Act, 1961 through Finance Act, 2011 to provide that period commencing from the date on which a reference for exchange of information is made by the competent authority under a DTAA/TIEA and ending with the date on which the information so requested is received by the Commissioner or a period of six months, whichever is less, shall be excluded. As in a number of cases the period in which information is received from a foreign jurisdiction exceeds six months, the law may be amended to exclude the entire period taken to receive the information. In addition, a further period of 60 days may be provided after receipt of information for completion of assessment proceedings to enable the AO to confront the assessee.

12.6 Section 115BBA is a presumptive section for calculating income of non-resident sportsmen (including athlete) or sports association. Similarly, section 194E allows withholding of tax at source from the income of non-resident sportsmen (including athlete) or sports association. However, the scope of these two sections is very limited when compared to Model Article 17 of the DTAA which covers not only the sportsmen but also entertainers in theatre, motion picture, radio or television artiste, or a musician. They are currently outside the purview of section 115BBA as well as 194E. Thus the presumptive taxation of 10% on gross income cannot be applied and also there is no provision of withholding. It would be proper that they are clubbed with sportsmen under the Income-tax Act as they are clubbed under the DTAA's to bring synergy between DTAA's and Income-tax Act and such persons under the tax net.

12.7 In the Direct Taxes Code Bill, a reporting requirement has been proposed making it obligatory for resident assesseees to furnish details of their investments and interests in any entity outside India in the form and manner as may be prescribed. In the return form under the present Income Tax Act also, provision may be made for resident taxpayers to furnish details of their investments and interests in any entity outside India, as their global income is taxable in India.

12.8 Government has taken several steps on the issue of black money of Indian citizen stashed abroad. One of the handicaps in the law is that there is no requirement to report foreign bank accounts in the tax return. There is a need to provide for such a reporting mechanism along with strict penalty for non compliance or wrong reporting. This will strengthen the fight against tax evaders who are parking black money abroad. In the proposed Direct Taxes Code, as per clause 113(2), the specified assets for the purposes of wealth tax include

- (i) *deposit in a bank located outside India, in case of individuals and Hindu undivided families, and in the case of other persons any such deposit not recorded in the books of account;*
- (j) *any interest in a foreign trust or any other body located outside India (whether incorporated or not) other than a foreign company; and*
- (k) *any equity or preference shares held by a resident in a controlled foreign company, as referred to in the Twentieth Schedule.*

The purpose of this provision is to have a reporting requirement of assets held abroad. This reporting requirement should include all investments made outside India by all the categories of taxpayers. This provision may be inserted in the present Wealth Tax Act also.

12.9 Section 115BBD has been amended in the Finance Act, 2011 to provide that dividends received by an Indian company from its foreign subsidiaries will be taxable at a reduced rate of 15%. This provision may be used for laundering of the black money stashed abroad and may be brought back to India through foreign subsidiaries of Indian companies as dividends after paying tax only at 15%. In addition to seriously jeopardizing our efforts in combating the menace of black money, this amendment is being seen by many honest taxpayers as a tax amnesty scheme benefiting tax evaders. This amendment may be withdrawn.

12.10 The report of the Committee on making amendments in Transfer Pricing Law in India may be implemented to curb the generation of black money through transfer pricing. Legislative amendments similar to introduction of a Foreign Account Tax Compliance Act (FATCA) passed in USA recently may be considered.

#### I. General Anti Avoidance rules (GAAR)

12.10.1 The GAAR has been provided in clause 123 of the Direct Taxes Code Bill, 2010. In view of the fact that a large number of transactions are not coming into tax net due to schemes designed specifically for the purposes of avoidance of taxes, including in the cross-border transactions, and in view of the prescription prescribed by the Hon'ble Supreme Court in the case of Vodafone International Holdings BV vs. Union of India (hereinafter referred to as Vodafone case), it is proposed that the GAAR may be provided through the Finance Bill, 2012. Further, in the light of the Supreme Court's decision in the Vodafone case, it needs to be ensured that the provisions relating to GAAR should be suitably modified so that some of the observations made by the Hon'ble Court may not be interpreted in such a manner so as to make the GAAR provisions ineffective. It is accordingly proposed that after clause (f) of sub-section (1) of section 123 of the Direct Taxes Code Bill, following clause may be added as under:

“(g) looking through the arrangement or transaction including by disregarding the corporate structure or by lifting the corporate veil.”

12.10.2 As per section 291(9) of the DTC Bill, 2010, the provisions of section 123, relating to GAAR, will be applied, whether or not such provisions are beneficial to him. In other words, the provisions of GAAR will be applicable even if the taxpayer is a resident of a country with which India has a DTAA in which such provisions are not there, providing a limited treaty override. It is proposed that suitable changes may be made in sections 90 and 90A so that in the Income-tax Act also, there will be treaty override on applicability of GAAR provisions.

#### II. Limitation of Benefits

12.10.3 The Supreme Court in Vodafone case has held that the provisions relating to Limitation of Benefits (LOB) are matter of policy and thus in a way prescribed the legislature to introduce such provisions in the Income-tax Act and/or in the treaties. A decade ago, the Hon'ble Supreme Court had held that in absence of LOB clause in the DTAA between India and Mauritius, in contrast to the LOB provision in the Indo-USA treaty, the treaty benefits cannot be denied. Despite our best efforts, we have not been able to introduce LOB provision in the Indo-Mauritius DTAA as Mauritius does not agree for renegotiation of the treaty, resulting in substantial loss of revenue to the exchequer. Not only in Mauritian treaty, but in a number of our other DTAAs, there are no provisions for LOB and we have not been able to renegotiate these DTAAs due to resistance from those countries. The Supreme Court in Vodafone case has examined the absence of LOB provision in the India-Mauritius DTAA and held as under:

“We are, therefore, of the view that in the absence of LOB Clause and the presence of Circular No' 789 of 2000 and TRC certificate, on the residence and beneficial interest/ownership, tax department cannot at the time of sale/disinvestment/exit from such FDI, deny benefits to such Mauritius companies of the Treaty by stating that FDI was only routed through a Mauritius company, by a company/principal resident in a third country; or the Mauritius company had received all its

funds from a foreign principal/company; or the Mauritius subsidiary is controlled/managed by the Foreign principal; or the Mauritius company had no assets or business other than holding the investment/shares in the Indian company; or the Foreign Principal/100% shareholder of Mauritius company had played a dominant role in deciding the time and price of the disinvestment/sale/transfer; or the sale proceeds received by the Mauritius company had ultimately been paid over by it to the Foreign Principal/ its 100% shareholder either by way of Special Dividend or by way of repayment of loans received; or the real owner/beneficial owner of the shares was the foreign Principal Company.”

12.10.4 Thus, the Supreme Court has held that almost in no case, treaty benefit can be denied to Mauritian companies, till the DTAA is revised or at the least, a LOB clause is introduced. It is accordingly proposed that Circular No. 789 of 2000, which has been issued by the CBDT, should be withdrawn. However, only the withdrawal of circular would have no effect, if the ratio of the above decision is applied. In view of the above, it is proposed that LOB provision may be introduced in the Income-tax Act with a limited treaty override on this issue meaning that even if there are no LOB provisions in a particular treaty, the domestic law will take precedence. Accordingly, the following amendments are proposed by way of a proviso below sub-section (2) of section 90 and section 90A:

“Provided that the benefit of the Agreement, entered into under sub-section (1), shall not be available to a treaty resident, or with respect to any transaction undertaken by such treaty resident, if the main purpose or one of the main purposes of the creation or existence of such a treaty resident or of the transaction undertaken by such treaty resident, was to obtain benefits under the Agreement that would not otherwise be available.”

12.10.5 The term “treaty resident” would then have to be defined in Explanation (below Explanation 2) of section 90.

“Explanation 3: For the purposes of this section, the term ‘treaty resident, means resident of a country outside India, or specified territory outside India, with which an agreement has been entered into under sub-section (1).”

12.10.6 Similarly the term “treaty resident” would have to be defined in Explanation (below Explanation 2) of Section 90A.

“Explanation 3: for the purposes of this section, the term ‘treaty resident’ means resident of a specified territory outside India, with which an agreement has been entered into under subsection (1).”

### III. Measures to prevent Round Tripping

12.10.7 The Hon’ble Supreme Court in the Vodafone case had observed that instances are also there when individuals form offshore vehicles to engage in risky investments, through the use of derivatives trading, etc. and many such companies do, of course, involve in manipulation of the market, money laundering and also indulge in corrupt activities like round tripping, parking black money or offering, accepting etc., directly or indirectly bribe or any other undue advantage or prospect thereof. After discussing in detail, the tax havens, treaty shopping and shell companies, it states in para 106 of the decision that the facts stated above are food for thought to the legislature and adequate legislative measures have to be taken to plug the loopholes. In the last two years, we had renegotiated a number of our existing DTAAAs for bringing them to the international standards on transparency and exchange of information for tax purposes and it is expected that in the coming years, we will be receiving information from a number of such jurisdictions. Similar results are expected from the Tax Information Exchange Agreements (TIEAs) we had entered into with some of the well-known tax havens such as Cayman Islands and British Virgin Islands. However, even if we receive the requisite information, the present provisions in the Income-tax



Act may not be sufficient to bring to tax the income which has been round-tripped or the black money which has been parked abroad. In view of the above, it is proposed that if the taxpayer has received foreign investment in the form of capital or long term loan or debentures, by whatever name known, above a prescribed limit, or has received deposits or donation above a prescribed amount, it will be required to furnish the details of the beneficial owner of the concern/entity making the investment/deposits/donations. The term "beneficial owner" may be defined in similar way as used in the PMLA, that is, the beneficial owner shall mean the natural person who ultimately owns or controls the person making donation or deposit or investment as the case maybe and the person on whose behalf the transaction is being conducted, and includes a person who exercises ultimate effective control over a juridical person. It may be noted that the Financial Action Task Force (FATF) has given 40+9 recommendations to prevent money laundering. These recommendations have been endorsed by 180 countries and jurisdictions and are recognized as Anti Money Laundering/Counter Terrorism Financing Standards. The recommendation No.5 of the FATF recommendations deals with the concept of beneficial ownership. The reporting requirement of the beneficial ownership will work as deterrence for the money laundering and tax evasion as the taxpayers will be required to report the beneficial owners of the foreign investments. It is proposed that section 68 may be amended to provide that if a taxpayer receives the above referred to foreign investment or donation, the burden lies on him to prove the identity of the beneficial owner, his genuineness and his credit worthiness. The draft amendment is proposed as under:

"Explanation: For the removal of doubts, it is hereby clarified that onus is on the assessee to offer explanation about the nature and source of the sum found credited in the books, where the sum credited represent donation or deposits or investment in the form of capital or loan or debenture, by whatever name known, including explanation with regards to the

- (i) Identity of the beneficial owner of the person making donation or deposit or investment of the case maybe;
- (ii) Creditworthiness of the beneficial owner of the person making donation or deposit or investment, as the case maybe; and
- (iii) Genuineness of the transaction.

The term "beneficial owner" shall mean the natural person who ultimately owns or controls the person making donation or deposit or investment as the case maybe, and the person on whose behalf the transaction is being conducted, and includes person who exercises ultimate effective control over a juridical person."

## ANNEX-A1

Federation of Indian Chambers  
of Commerce and Industry



January 12, 2012

Mr Shishir Jha  
CIT (Investigation)  
Central Board of Direct Taxes  
Ministry of Finance  
New Delhi

Dear Mr Jha,

### Suggestions for Curbing generation of Black Money

This is in response to your fax letter No.291/15/2011-IT (Inv.I) dated 30<sup>th</sup> December, 2011, inviting FICCI's suggestions for curbing generation of black money in India.

Based on the inputs received from our constituents, we would like to submit as under:-

- FICCI supports the efforts of the government to curb the menace of black money. The problem of tax evasion has been a subject matter of focus by many countries. Recently, Tax Justice Network, a London based watchdog that fights against tax havens, published a study on the subject. It suggests that the size of the shadow economy ranges from 8.6% in the USA to 11% in Japan to 27% in Italy, 39% in Brazil and 43.8% in Russia. For a developing economy like India, the loss of tax revenues lost as a result of the shadow economy is significant and this can have a material bearing on the future development of the economy.
- Whilst there are several measures that can be taken to reduce the size of the shadow economy, the one key issue is the use of technology. While a lot of effort has gone in this direction, the ability of the revenue to link up the Annual Information Reports filed by corporate, the exemption claims made, the lower withholding certificates filed, etc is a key link to tracking the flow of funds and plugging elements of shadow economy.

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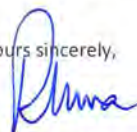
- 2 -

- Currently, there are restrictions on the deductibility of cash expenses, cash deposits and repayments of deposits in cash. **There is, however, no restriction on personal expenditure in cash.** This is one key area where cash is deployed. Payments in cash for household purchases, electronics, etc is an area which is not plugged and is a channel for the parallel economy to flourish. **The government should consider provisions that all payments beyond a particular limit should be only through credit cards/bank instruments.** This could be introduced initially in the cities and spread over a period of time to other locations.
- The government should also **evolve suitable strategies** to stop generation and perpetuation of new black money through **controlling fresh cash expenditure, real estate transactions, and to bring into main stream the past accumulated cash.**
- Goods and Services Tax (GST) when finally introduced, **would act as a great deterrent** for individuals and companies **to avoid payment of taxes.**
- Finally, the government should **consider announcing one time amnesty scheme,** to motivate Indians to bring back their funds lying overseas.

We trust, the above will help in curbing the generation of black money.

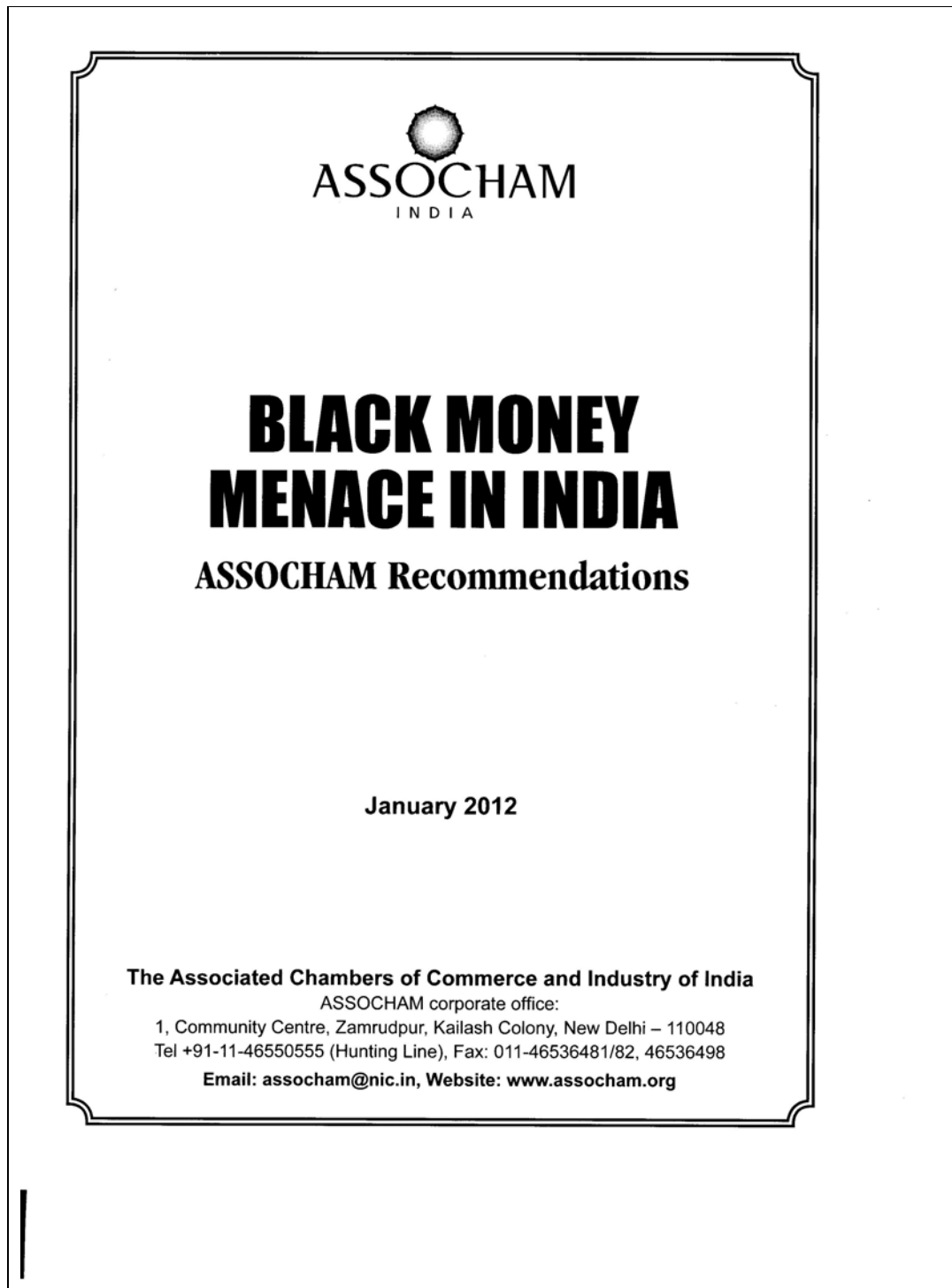
With best regards

Yours sincerely,



Rajiv Kumar

ANNEX-A2



## ACKNOWLEDGEMENT

The ASSOCHAM President, Mr. Dilip Modi, in September 2011 appointed an expert committee to study and recommend realistic strategy to the Government of India on the issue of black money. The committee was chaired by Mr. Ved Jain, Chairman, ASSOCHAM National Council on Direct Taxes and former President, Institute of Chartered Accountants of India, and co-chaired by Mr. R. K. Handoo, Chairman, ASSOCHAM Legal Affairs Council and an eminent Supreme Court Advocate. The committee comprises of luminaries from industry, legal, professional and social sector as its members.

ASSOCHAM hopes that the Government will find the recommendations / suggestions of the committee very useful.

January 2012



D. S. Rawat  
Secretary General  
ASSOCHAM

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## BLACK MONEY MENACE IN INDIA

### I INTRODUCTION

Individuals and institutions globally are engaged in evading taxes and generating surpluses which do not get accounted for in the formal economy. These funds are generated from activities which may be legal or illegal by nature. However the mere fact that taxes have not been paid on such incomes, as per the rules of the land, converts such funds to form a part of the parallel economy or Black Money generation. The fund generated is normally held as currency notes and/or assets through investments in gold, jewellery, precious stones, art and artifacts, real estates and others. The literature revealed that strong parallel economies are created due to high level of corruption and weak hold of regulatory mechanism in developing regions of the world.

The Wanchoo Committee stated that 'the term Black Money is generally used to denote unaccounted money or concealed income and/or wealth as well as money involved in transactions wholly or partly suppressed'.

In India, Kaldor's estimates for black money generation in 1953-54 were about Rs. 600 crores (i.e. 6% of National Income then) on account of tax evasion only. Some other estimates further put the black money generated in India annually as Rs. 700 crore (1961-62); Rs. 1,000 crores (1965-66); Rs. 1,400 crores (1968-69). Estimates by Dr. Rangnekar for the same periods were Rs. 1,150 crore, (beginning of 1960s) Rs. 2,350 crore (mid 1960s) and Rs. 2833 crore by the late 1960s.

The Indian Institute of Finance study indicated that the growth rate of black money in 1991 has been at a rate of Rs. 60,000 crores per year. N. Vittal, Former Indian Chief Vigilance Commissioner in 2002, estimated that the yearly growth rate of Black money is a factor to the tune of 40-50 percent of GDP growth in the Indian economy on a year to year basis.



Another concept that has close proximity to Black money is the money laundering. The term laundering is referred to as investment or other transfer of money flowing from racketeering, drug transactions and other sources (illegal sources) into legitimate channels so that its original source cannot be traced. The traditionally known activities for laundering of money are via drugs, racketeering, kidnapping, gambling, procuring women and children, smuggling (alcohol, tobacco, medicines), armed robbery, counterfeiting and bogus invoicing, tax evasion and misappropriation of public funds.

Both black money and money laundering result in capital flight. Capital flight may be defined as transfer of assets denominated in a national currency into assets denominated in a foreign currency, either at home or abroad, in ways that are not part of normal transactions. One technique that can be used to move significant amounts of capital out of a country is the over-invoicing of imports and the under-invoicing of exports.

It may be noted that that illicit flows differ from the broadest definition of capital flight which also includes "normal" or "legal" outflows due to investors' portfolio choices. Specifically, illicit flows are comprised of funds that are illegally earned, transferred, or utilized — if laws were broken in the origin, movement, or use of the funds then they are illicit. The transfer of these funds is not recorded anywhere in the country of origin for they typically violate the national criminal and civil codes, tax laws, customs regulations, VAT assessments, exchange controls, or banking regulations of that country.





## II

### CORRUPTION AND CAPITAL FLIGHT: EMPIRICAL ASSESSMENT

An important study conducted by Quan and Rishi (2006) empirically examined the role of corruption in impelling capital flight. Corruption was broadly defined as the abuse of public office for private gain. There is an implicit belief that popular mechanisms of capital flight, such as bribes and kickbacks on government contracts, trade misinvoicing, outright cash transfers, and smuggling are instances of corruption in the broadest sense. Identifying corruption as one dimension of poor governance, the empirical analysis explores direct linkages between corruption and capital flight in a broad sample of countries. The study hypothesized that: Does corruption impel capital flight by raising the risk of domestic investment, *ceteris paribus*? This hypothesis was tested for a panel of 69 countries over a seven-year period from 1995–2001. In this regard the study mentioned that,

- Political instability and poor governance contribute to a domestic environment that deters investment and induces capital flight.
- Corruption works as a regressive tax – the poor pay a disproportionate share of their income in the form of bribes to secure access to public services.
- Bribes and official extortion act as an extra tax and therefore deter potential foreign direct investment into developing countries. Corruption acts as a source of macroeconomic vulnerability and lower economic growth.

Governance is understood to have six dimensions: voice and accountability; political stability and the absence of major violence; government effectiveness; regulatory quality; rule of law; and the control of corruption. The panel data analysis of corruption and capital flight indicated a positive and significant effect of corruption on capital flight. Especially, it suggests that an increase in corruption by one standard deviation induces an increase of almost 2 percent in capital flight.



## III

## HOW TO ESTIMATE CAPITAL FLIGHT

The World Bank method compares the sources of external finance (the change in external debt and net foreign direct investment), with the uses of finance (current account deficit and the change in official reserves). Sources of funds exceeding recorded uses of funds reflect unrecorded outflows. Sources of funds include increases in net external indebtedness of the public sector and the net inflow of foreign direct investment. Uses of funds include financing the current account deficit and additions to reserves. In this broad macroeconomic framework, illicit outflows (inflows) exist when the source of funds exceeds (falls short of) the uses of funds. Thus:

(Source of Funds) - (Uses of Funds)

$$\text{Illicit Outflow} = [\Delta \text{ External Debt} + \text{FDI (net)}] - [\text{Current Account Balance} + \Delta \text{ Reserves}]$$

The above model estimates are adjusted for trade mispricing, which has been long recognized as a major conduit for capital flight. The underlying rationale is that residents can shift money abroad illicitly by over-invoicing imports and under-invoicing exports. In order to capture such illegal transactions, a developing country's exports to the world (valued free on-board (f.o.b.) in US dollars) are compared to what the world reports as having imported from that country, after adjusting for the cost of insurance and freight. Similarly, a country's imports from the world net of freight and insurance are compared to what the world reports it has exported to that country.



#### IV

#### THE CURRENT ISSUES

Tax evasion is one of the major reasons for the creation of an underground economy. There are 70 tax havens and secrecy jurisdictions and that there are millions of dummy corporations that shield the owner's identity. Through transfer pricing, false documentation, fake corporations, tax havens and secrecy jurisdictions, Western banks and businesses handle \$ 1 trillion of illicit proceeds every year. Assets in tax havens are estimated at \$ 11.5 trillion and for every \$ 1 that poor countries receive in foreign aid, an estimated \$ 10 flows abroad through illicit transfers. There is capital flight from developing and transition countries to developed countries to the extent of \$ 500 billion every year. In December 2008, GFI produced a report that was even more specific. For this five-year period between 2002 and 2006, this study estimated that illicit financial flows from developing countries amounted to between \$ 850 billion and \$ 1.06 trillion a year. This capital flight occurred through trade mispricing, criminal and commercial smuggling (drugs, minerals, contraband goods) and mispriced asset swaps.

Thanks to OECD and G-20 pressure, several tax havens have now changed their policies. There is an OECD list of tax havens and financial centres that have already implemented the standards, or have committed to the standards, though they are yet to implement them. One example is in Switzerland. Swiss banks used to be bound by the Banking Law of 1934. Traditionally, Swiss law distinguished between tax evasion and tax fraud. The latter had direct criminal intent and international tax cooperation used to be provided only when there was tax fraud, not when there was tax evasion. But because of G-20 and OECD pressure, the Swiss have eliminated this.

All G20 governments have now agreed to a multilateral Convention to tackle tax evasion more effectively. The Multilateral Convention on Mutual Administrative Assistance in Tax Matters offers a wide range of tools for cross-border tax co-operation. It includes automatic exchange of information, multilateral simultaneous



tax examinations and international assistance in the collection of tax due. At the same time, the Convention imposes safeguards to protect the confidentiality of the information exchanged.

India has 83 double tax avoidance agreements (DTAAs) and another 20 countries with which it has limited tax agreements. But the point is that DTAAs do not necessarily have clauses on the exchange of tax information. Therefore, India needs to sign tax information exchange agreements (TIEAs) urgently, especially because the global climate has changed in favour of such TIEAs. At present, India only has one TIEA, signed with Bermuda on 7th October 2010. Another 22 TIEAs are reportedly being renegotiated. The Finance Minister outlined a five-pronged strategy for handling the problem of black money: (1) Join the global crusade against black money; (2) Create an appropriate legislative framework; (3) Setting up institutions for dealing with illicit funds; (4) Developing systems for implementation; and (5) Imparting skills to manpower for effective action. This strategy, with the inclusion of the TIEAs, is unexceptionable. But it is preventive. Even when a TIEA is signed, it is likely to be prospective, not retrospective. That is, such a strategy handles the problem of future flows of illicit capital flight. It doesn't address the problem of Indian money that is already abroad. Those are valuable resources and, if brought back, can be used to fund India's physical and social infrastructure needs.



## V

## THE EVOLVING GLOBAL FRAMEWORK

Several countries are currently operating voluntary compliance programmes. Such rules or programmes provide an opportunity to facilitate compliance in a timely and cost effective manner, saving costly and contentious audits, litigation and criminal proceedings. Voluntary compliance initiatives must walk a fine line between providing sufficient incentives for those engaged in noncompliance to come forward and not rewarding or encouraging such conduct. Offshore voluntary compliance programmes offer the opportunity to maximize the benefits of improvements in transparency and exchange of information for tax purposes, to increase short-term tax revenues and improve medium-term tax compliance.

The increase in the risk of detection through improved international tax co-operation coupled with the availability of voluntary disclosure programmes has lead to a large number of taxpayers coming forward and significant amount of tax being collected. For instance, more than 14,700 taxpayers took advantage of a recent US initiative and in Germany more than 20,000 taxpayers made a voluntary disclosure resulting in reported additional revenue to the German government in the range of 4 billion Euros.

Table 1 gives a bird's eye view of the recent initiatives taken by different countries to improve offshore compliance and their results.

**Table 1**  
**Recent Country Initiatives to Improve Offshore Compliance**

Country	Action taken to build on the G20 initiative	Amount Disclosed and Taxes Paid
Argentina	Voluntary Disclosure Initiative (2009)	EUR 146 million additional revenue yield.
Australia	Offshore Voluntary Disclosure Initiative (2010/2011)	EUR 150 million (AUD 210 million) additional revenue assessed. More than 8 000 taxpayers involved.



Brazil	Voluntary Compliance Initiative (2009)	Estimated EUR 315 million additional revenue yield.
Canada	On-going Voluntary Disclosures Program (fiscal years ending in 2009-2011)	EUR 620 million (CAD 860 million) total unreported income disclosed. 8,700 disclosures.
China	Broadening the network of tax information exchange agreements and increasing numbers of requests.	EUR 80 million (CNY 690 million) additional revenue yield (in 2010), expected to grow significantly.
Denmark	"Project havens" aimed at uncovering hidden wealth and income abroad.	More than EUR 50 million additional revenue yield so far.
France	Offshore Voluntary Disclosure Initiative (2009)	EUR 1.2 billion additional revenue yield. More than 4 700 taxpayers involved.
Germany	Voluntary Disclosures (2010/2011)	Estimated additional revenue yield of EUR 1.8 billion. Between 25 000 and 30 000 taxpayers involved.
India	Increase of staff number, greater co-operation with G20 partners, increase in exchange of information agreements.	Significant additional revenues expected over next two years.
Ireland	Voluntary Disclosures (since 2009)	EUR 70 million additional revenue yield. Around 400 taxpayers involved. An earlier initiative yielded over EUR 1 billion.



Italy	Offshore Voluntary Disclosure Initiative (2009/2010)	EUR 5.6 billion additional revenue yield. Total undisclosed assets: EUR 104.5 billion. Representing five times the amount from the 2002/2003 initiative.
Korea	Establishment of the Offshore Compliance Enforcement Centre (2009) and offshore tax evasion cases uncovered through tax audits (since 2009)	EUR 510 million (KRW 810 billion) additional revenue assessed.
	Foreign Financial Accounts Reporting Program (2010)	More than 500 taxpayers involved.
Mexico	Offshore Voluntary Disclosure Initiative (2009)	EUR 58 million (MXN 1,057 million) additional revenue yield. Total undisclosed assets: EUR 1,073 million (MXN 19,436 million).
Netherlands	Voluntary disclosure program on offshore accounts	EUR 475 million additional revenue yield so far. More than 9 000 taxpayers involved.
	Tackling the diversion of profits resulting from the transfer of intangibles by individuals and SMEs to no or nominal tax jurisdictions	EUR 20 million additional revenue yield so far and expected to raise EUR 150 million over a 10 year period.
Norway	Voluntary Disclosures	EUR 30 million additional revenue
Portugal	Exceptional Regime of Tax Regularization of Assets (2009)	EUR 83 million additional revenue collected. Around 1 000 taxpayers involved.



South Africa	Voluntary Disclosure Program (2010)	EUR 22 million additional revenue yield (ZAR 229 million)
Spain	Compliance Initiatives focused on Individuals	EUR 260 million additional revenue yield
Turkey	Offshore Voluntary Disclosure Initiative (2009)	EUR 225 million additional revenue yield (TRY 558 million). Total undisclosed assets: EUR 11.25 billion (TRY 27.9 billion).
United Kingdom	Liechtenstein Disclosure Facility	EUR 160 million additional revenue yield (GBP 140 million). More than 1 350 taxpayers involved.
	New Disclosure Opportunity	EUR 100 million additional revenue yield (GBP 85 million). Approximately 5 500 disclosures.
United States	Offshore Voluntary Disclosure Initiatives (2009 and 2011)	EUR 2 billion additional revenue yield (USD 2.7 billion) recovered thus far from the 2009 and 2011 initiative. More than 30 000 taxpayers involved.
	Switzerland Disclosure (2009)	Disclosure of 4 450 accounts.

Source: Organisation for Economic Development (2011) 'The Era of Bank Secrecy is Over', October 26,





**VI**

**ESTIMATES OF ILLICIT FINANCIAL FLOWS FROM INDIA**

There are no official estimates of black money in India. All the estimates made by the non-government sources though indicate generation of large amounts of black money in India, there exists a large variation about the amount of black money. For instance, the Bureau of International Narcotics and Law Enforcement Affairs of United States Department of State in its Report on 'Money Laundering and Financial Crimes' Vol.2, published in March 2010, observed that private analysts estimate India's black market to range from \$2.1 - \$2.5 trillion.

Prof. R.Vaidyanathan, Professor of Finance, Indian Institute of Management, who worked on the subject of 'Tax havens and Illegal Funds of India', quoted that the amount of the Indian money stashed abroad may be of the order of \$1.4 trillion.

Agarwal and Agarwal observed that during the period 1995-2009, illicit financial flows from the Indian non-bank private sector into developed country banks and offshore financial centers (OFCs). Indian private sector shifted away from bank deposits to deposits in OFCs. As the share of OFC deposits increased from 36.4 percent of total deposits in 1995 to 54.2 percent in 2009, deposits in banks fell commensurately to 45.8 percent in the last year. As OFCs are subject to even less oversight than banks and typically hold a larger share of illicit funds, the increasing recourse to OFC deposits relative to banks could be symptomatic of the burgeoning underground economy in India from which such funds emanate.

A more recent study, Kar, Dev and Cartwright-Smith (2008), India lost between US\$23.7-\$27.3 billion annually in illicit financial flows (IFFs) during 2002-2006.

Shankar Acharya and his colleagues at the National Institute of Public Finance and Policy (NIPFP) undertook what is still the most comprehensive study on the size of the black economy in India. Stated simply, this study found that the size of the black economy in India was less than 30% of GDP and was more like 21%. A



subsequent study by Arun Kumar placed it at 35%. There are estimates of around 50% that also float around.

"All these estimates are based on various unverifiable assumptions and approximations. Government has been seized of the matter and has constituted a multidisciplinary committee to get studies conducted to estimate the quantum of illicit fund generated by Indian citizens." This is a statement from the Finance Minister's Press Conference on 25th January 2011.



**VII**

**ASSOCHAM VIEWS & RECOMMENDATIONS**

In view of the current relevance of the subject, ASSOCHAM organized a series of internal meetings. The outcomes of these meetings are as follows:

- A. ASSOCHAM is of the view that the generation of the black money in the country is mainly due to the following factors:

**i. Real Estate Transactions:**

It is a common knowledge that most of the real estate transactions are understated. There are several reasons for the same. However, the main reason for understatement of the real estate transactions is the high rate of stamp duty levied on registration of the property. Further at the time of the resale there is no system of allowing credit of the stamp duty paid at the time of purchase.

**Suggestions:**

- (a) Therefore, there is a need to introduce a uniform stamp duty rate applicable across the country. ASSOCHAM is of the view that a stamp duty rate of 3% is fair and reasonable rate with the benefit of allowing credit of the stamp duty paid at the time of the purchase.
- (b) It is further recommended that the mechanism of determination of circle rate being notified by each of the States also be streamlined. The circle rate needs to be notified every year on the basis of the data input for the preceding year so as to make sure that the circle rates are as good as the prevalent market rate.
- (c) ASSOCHAM is of the view that reduction in the stamp duty rate with credit of the stamp duty paid at the time of the purchase will not have any impact on



revenue collection of the State Governments and will go a long way in curbing the menace of black money.

**ii. Expenditure on Elections:**

One of the main factors contributing to the parallel economy in the form of black money is the huge expenditure required to be incurred on elections. In the country, we have elections not only for the Parliament but also for the State Assemblies, Municipal Corporations, Panchayats as well. It is a common knowledge that candidates spend huge amount of money in the elections and most of such money is unaccounted money. The reason for this unaccounted expenditure are two fold – i) the restriction on the total amount of the expenditure a candidates is legally allowed to spend, and ii) absence of legitimate source of income in the hands of the candidates contesting elections.

Addressing these issues and ensuring transparent way of financing the democracy has long been part of the public debate. Country has remained a distant onlooker debating the issue. A vague idea of how big this problem is, can be had from the fact that on an average about Rs.10 Crore per Parliament seat is the expenditure incurred by the candidates contesting the elections and about Rs.5 Crore is the expenditure incurred by the candidates contesting the State Assembly elections. Assuming that elections are being held once in five years, the total expenditure being incurred by the candidates for Parliament and Assembly Elections itself will be more than Rs.25,000 Crore. Besides this a huge amount of expenditure is being incurred on elections to the Municipal Corporations and Panchayats also.

The Election Commission has fixed unrealistic Cap of Rs. 40 lakhs per parliament seat and Rs.16 lakhs per Assembly seat.

The world's leading democracies such as US, UK and Germany have enacted laws relating to public funding of the elections.



Chamber is of the view that it is high time that the country enacts laws relating to public funding. Further there is a need to consider the ground realities while fixing the ceiling of expenditure a candidate can spend in the elections.

**iii. Misuse of discretion by the public authorities:**

There's a lot of hue and cry in the country on account of corruption, which is due to the misuse of discretion by the public authorities. This misuse of discretion by public authorities has led to the generation of a lot of black money in the system, which cannot be accounted for by the public authorities and which either gets stashed abroad or finds its ways in the undervalued properties and gems and jewellery.

The Chamber is of the view that the discretion of the public authorities can be controlled by infusing extreme accountability in the system where the public authority would be liable to pay penalty/fine for any misuse of discretion.

**iv. Import of gold and consumption in the country thereof:**

India is the biggest consumer of gold in the world. The import of gold is on payment of hard earned foreign exchange while the sale of gold at the grassroots level is mainly in cash, leading to generation of huge black money. Therefore, there is an urgent need for a mechanism to curb it.

**v. Tax Haven Countries:**

One of the reasons of generation of black money is the easy parking of such funds in tax haven countries. Post-independence India has passed through toughest tax laws and foreign exchange regulations. The extreme high rate of taxation, may it be income tax, excise duty, customs encouraged people more and more people to carry out the transactions outside the books of account and in the result generate black money. The black money so generated over the period has been parked either in the tax haven countries or the countries where the secrecy laws ensure that money so parked will not be detected.



#### **vi. Foreign Exchange Restrictions**

The strict restriction on allowing foreign currency in case of need had also encouraged people to park funds outside the country in foreign currency so as to meet the requirements or the obligations may it for business, education, health and other personal purposes.

- B.** Post-liberalization, however, there have been substantial reforms in the taxation laws and the tax rates have been moderated to a reasonable level. The foreign exchange laws have also been liberalized so that one does not have much difficulty in obtaining foreign currency in case of need be, may it for business, education, health or for any other purposes. Thus, as on date there is not much incentive to park funds outside the country.

#### **C. How to Bring Back the Money Parked Outside**

The main issue is how to bring back the funds a substantial part of which got parked outside India during the pre-liberalization regime. The persons who have parked these funds outside India will not bring it back because of the penal actions which they may have to face. At the same time the Government cannot detect such funds in the absence of any information though discussions have been going on with the various countries and agreements have been entered into to exchange information under the Double Taxation Avoidance Agreements. Further the fact remains that such exchange of information will be perspective and practically as well as legally it will not be possible to get information about the past activities and the funds stashed away abroad in the past.

In view of these ground realities it will be prudent that Government of India opens a window so that this money can be brought back to India. In this context, following measures are suggested:

- (i) ASSOCHAM is of the view that while opening this window it will be important to provide immunity to the person declaring such assets which



can be in the form of bank deposit, investment in shares/debentures, mutual funds, property, etc.

- (ii) The immunity needs to be provided under Direct Tax and Indirect Tax Laws, Companies Act, Foreign Exchange Management Act including Money Laundering Act etc.
- (iii) As regards the tax to be paid on such disclosure of money, the Chamber is of the view that a flat rate of 40% be levied on the present value of such money or the asset.
- (iv) The cutoff date for valuation be fixed may be 1.1.2012 or 1.4.2012. Foreign currency and deposits to be valued by applying the notified exchange rate as on the valuation date.
- (v) Further 10 % of the amount be asked to be invested in Infrastructure Bonds of 7 years tenure.
- (vi) The funds so collected to be earmarked and used by the Government only for the development of the Infrastructure.
- (vii) This high rate of tax (at the rate of 40%) with further investment of 10 per cent in Infrastructure Bonds as compared to present maximum tax rate of 30% will help ensuring that there is no misuse of the scheme by unintended persons.
- (viii) Further charging tax on the present value of the foreign assets by applying the current exchange rate will also ensure that this amnesty scheme is not exploited by unscrupulous people by converting black money in to white by paying nominal taxes.

These two measures, the Chamber is of the view, will address all those issues which have arisen in the earlier voluntary disclosure scheme.

ASSOCHAM while making this proposal of amnesty is conscious of the fact that tax evaders should not get go away and be shown any leniency. However



at the same time the ground realities cannot be ignored. The fact remains that as on date it may not be possible to get hold of these persons who have stashed money abroad that is why the scheme is an invitation to these people to come forward and pay taxes.

- Further this scheme shall not be applicable in respect of those persons where the authorities have detected unaccounted money and proceedings have been initiated before the date when such scheme is notified.
- That the objective of this amnesty scheme is to get back the money stashed abroad but considering the fact that there may be frequent cross and inter linked transactions and it may not be possible to isolate the transactions with respect to foreign bank account or the foreign assets, the scheme be made open for money being kept abroad as well as in India.
- Further there may be instances where money remitted abroad has been utilized and not available for repatriation. As such there should be no insistence in such cases to bring money back.
- This window may be kept opened for a minimum period of six months.

ASSOCHAM is of the view that looking to the conscious and the debate which has arisen in the last few years and the efforts being put in by the Government to collect information about the foreign assets help the public, there will be a large number of people who will like to come forward voluntarily and to make such disclosures and bring back the money in the country.

The Chamber is also of the view that if the above scheme is implemented in right earnest then a substantial part of the funds parked abroad for which the estimate ranges from few hundred billion dollars to few thousand billion dollars may get covered in the Scheme which will help the country not only meet its Revenue deficits but also help in meeting the Balance of Payment (BOP).

ASSOCHAM on its part assures that it will put all its efforts to make the scheme successful.



## ANNEX-A3

### **Gist of Feedback on Black Money from Public**

- 1 a) Make stringent laws.  
b) There should be community policing.
- 2 Those who are having accounts abroad must be given life imprisonment without mercy & delay.
- 3 CCTV cameras 24 hours for all government officials - police/lawyers/judges/doctors/sales tax officers/MLAs/CMs/PM etc.
- 4 Minimize paper currency and increase electronic money (cards).
- 5 Strict laws and its strict implementation without distinction between prominent personalities/politicians and ordinary people.
- 6 a) Strict law.  
b) To convert all black money as national property.  
c) Penalty - special tax.
- 7 a) Postal transactions using e-credits/online transactions.  
b) Stop currency notes of Rs.500/- & Rs.1000/-.
- 8 Scrutinise the admission fees of private schools in Surat.
- 9 a) Reduce stamp duty, capital gains tax.  
b) Make bonds always available for tax free investment at lucrative terms.
- 10 Politicians are corrupt.
- 11 a) Encourage online payments.  
b) Integrate all land/property registrations/property tax payments/I.T. Department records/Banks to assist digging out date and analysis to ascertain avoidance of tax.
- 12 Bring down corruption.
- 13 a) Declare black money as national property.  
b) Detect and stop transfer of black money abroad.  
c) Will require to unearth black money as it mostly belongs to politicians, bureaucrats and businessmen.
- 14 a) Declare black money as national money.  
b) Guilty to be sent to jail for life time.
- 15 Confiscate black money obtained through bribery and corruption.
- 16 Implement strict rules and laws.
- 17 a) Declare black money as India's property.  
b) Punish the guilty.

- 18 Penalise the guilty.
- 19
  - a) Attach properties procured from illegal money in India.
  - b) Declare them as assets of the country.
- 20 Politicians should declare their assets before elections as they are ones who have most black money.
- 21
  - a) Form a special team to unearth black money.
  - b) Encourage informers with 10% - 15% of total black money.
  - c) Severe punishment to the guilty.
  - d) Give a period to declare black money with no penalties on 50:50 basis.
  - e) Educate the children in schools about such subjects.
- 22 Income Tax system has failed.
- 23
  - a) Use CCTV in offices/authorise sting operations.
  - b) Punishment to the guilty.
- 24 Brought back black money to be used in reducing our foreign debt, loans etc. And extra if any, to be utilised for
  - a) Investment in education.
  - b) Investment in medical care for the poor.
  - c) Reduce oil prices.
- 25 To end corruption throw all Congressmen in jail and confiscate their property.
- 26
  - a) Fines and penalties to be most stringent.
  - b) An opportunity may be given to defaulters to bring back black money on 50:50 basis (government to collect 50% of the total black money and no penalty/punishment for a certain period.
- 27 Treat offenders as criminals/terrorists.
- 28 Black money should be brought back at all cost.
- 29
  - a) Black money to be traced and brought immediately.
  - b) Punishment to the guilty.
- 30
  - a) Get back all black money.
  - b) Improve our economy.
- 31
  - a) Declare black money as national property.
  - b) Harsh punishment to the guilty.
  - c) All assets purchased by black money be declared as national property.
- 32 Bring back black money without any penalty and then implement harsh laws to fight corruption.
- 33 Expose names of people who have black money.

- 34 Enact effective laws against black money and corruption.
- 35 Provide an opportunity one time free of penal action to bring back black money.
- 36
  - a) Create a special department to trace black money.
  - b) Grant 1% of black money as bonus to this department (to prevent it from being bribed).
  - c) Stringent penal laws to defaulters.
  - d) Mandatory jail term of one year.
- 37 If government acts and brings back black money in short period it will sent a strong message to the people.
- 38
  - a) Strong penal action against defaulters - passport impounded, properties attached.
  - b) All to be treated equally under the same applicable law.
- 39
  - a) Create awareness of negative effects of black money to public.
  - b) Give an opportunity to declare their black money.
- 40
  - a) Laws to handle corruption.
  - b) Govt. servants to be dismissed.
  - c) Create a national security number.
- 41
  - a) Black money in foreign banks to be declared as national property.
  - b) Pass a bill to bring back black money.
- 42 Imprisonment for ten years to defaulters.
- 43
  - a) If an Indian has an account in foreign bank and the balance is high - IT Department to be informed.
  - b) Strict laws and proceedings to be quick.
  - c) Politicians if defaulter - prevent from contesting elections.
  - d) Employees - private and government - to be suspended.
- 44
  - a) Simplify procedures and all dealings.
  - b) Lower Income Tax rates.
- 45 To cut short long drawn battle to bring back black money:
  - a) Tax exemption schemes for money brought back.
  - b) Some changes in FEMA act and rules.
- 46
  - a) Declare black money as national property.
  - b) Imprisonment for defaulters.
- 47
  - a) People dealing with black money issue to be honest, they should not cover up their black money.
  - b) Update the people of the developments.
- 48 Reduce stamp duty on house/flat registration.

- 49 a) People should disclose black money.  
b) Black money should be taxed heavily.
- 50 Transactions relating to sale/purchase of real estate's should be monitored more closely and publication of guidance value/cost relating to real estate's on a weekly basis to a certain registration charges like in USA.
- 51 a) Declare black money as national asset and confiscate it immediately.  
b) Offenders to be brought to book.
- 52 a) A stringent law and jail term for 10-20 years if committing such crime.  
b) Separate speedy courts for such cases.
- 53 Stringent action against defaulters.
- 54 a) Declare black money as national asset through ordinance/law.  
b) Constitute an independent monitoring agency to monitor and clean up the corrupt law enforcing agencies.  
c) Punishment for offenders to act as deterrent.  
d) Law enforcing agencies to be tech savvy and transparency required.
- 55 a) Include PM under Lokpal bill.  
b) Ceiling/limit of wealth of politicians and all those related to them.  
c) Limit the years to 10 years a person can be PM/CM.
- 56 a) Black money to be declared national asset.  
b) 5 - 25 year's rigorous jail without parole.  
c) All amounts to be recovered.  
d) Law makers all tainted - trying to save themselves.
- 57 The Government should act without fear of people involved and make public their names.
- 58 a) To have an international law which would require permission of the country's government for deposit in foreign banks.  
b) To spend the retrieved black money on infrastructure.
- 59 a) First assets of all politicians and government servants to declare if they and their families have Swiss accounts.  
b) Black money to be deposited with Finance Ministry as 100% tax.  
c) Minimum 10 years imprisonment.
- 60 Remove corruption black money will disappear.
- 61 a) Increase the work force of IT Department and conduct more raids.  
b) Strict punishment.
- 62 Remedy is Lokpal bill.
- 63 a) Bring back black money and use it for welfare of public.  
b) Strict action against defaulters/life imprisonment.

- 64
  - a) Bring back black money and put it to right use.
  - b) Act swiftly.
  - c) Stringent punishment for defaulters.
- 65
  - a) A law to punish who takes bribe and not giver.
  - b) recover expenses related to recovery from defaulters.
  - c) Opportunity to defaulter to convert black money to white money.
- 66 Retrieved black money to be used to benefit farmers.
- 67 Remove Rs.500/- & Rs.1000/- notes.
- 68
  - a) Annual foreign currency accounts to be filed directly with Finance Ministry.
  - b) Indian currency to be made fully convertible.
  - c) A list of black money earners should be released periodically with action taken reports.
- 69
  - a) Threaten defaulters to sue them.
  - b) Create an economic wing in the RAW and have an officer attached at each embassy to track money inflows and outflows.
- 70 Defaulters to be declared anti-national and publicly hang them to death.
- 71
  - a) Reduce tax rates and tax spending instead of income.
  - b) President of India - powers to be given to lead the mission of bringing black money back.
  - c) Implement voluntary disclosure schemes.
  - d) Educate the young ones on the evils of corruption.
- 72
  - a) All transactions above Rs.50,000/- through bank only.
  - b) De-notify the Rs.500/- & Rs.1000/- currency notes.
  - c) Give discounts on online and bank transactions initially for encouragement.

**TABLE-C1**

**Rank of select countries in  
Corruption Perception Index, 2011**

<b>Rank</b>	<b>Country</b>	<b>Score</b>
64	South Africa	4.1
73	Brazil	3.8
75	China	3.6
95	India	3.1
143	Russia	2.4

*Source: Transparency International ([www.transparency.org](http://www.transparency.org))*

**TABLE-C2****Ease of doing business ranking**

<b>Country</b>	<b>Ease of doing business (rank)</b>	<b>Starting a business</b>	<b>Dealing with construction permits</b>	<b>Getting Electricity</b>	<b>Registering property</b>	<b>Getting credit</b>	<b>Protecting investors</b>	<b>Paying taxes</b>	<b>Trading across borders</b>	<b>Enforcing contracts</b>	<b>Resolving insolvency</b>
<b>India</b>	<b>132</b>	<b>166</b>	<b>181</b>	<b>98</b>	<b>97</b>	<b>40</b>	<b>46</b>	<b>147</b>	<b>109</b>	<b>182</b>	<b>128</b>
Brazil	126	120	127	51	114	98	79	150	121	118	136
China	91	151	179	115	40	67	97	122	60	16	75
South Africa	35	44	31	124	76	1	10	44	144	81	77
Russian Federation	120	111	178	183	45	98	111	105	160	13	60
Indonesia	129	155	71	161	99	126	46	131	39	156	146
U.S.A.	4	13	17	17	16	4	5	72	20	7	15
U.K.	7	19	22	60	68	1	10	24	13	21	6
Singapore	1	4	3	5	14	8	2	4	1	12	2

Source: <http://www.doingbusiness.org/rankings> [World Bank]

TABLE-C3

## Growth in Currency and the Cash Economy



Source Annual Report of RBI – 2010-11



TABLE-C4

**Banknotes in Circulation**

Denomination	Volume (Million pieces) End - March			Value (₹ crore) End - March		
	2009	2010	2011	2009	2010	2011
1	2	3	4	5	6	7
₹2 & ₹5	7,865 (16.0)	7,953 (14.1)	11,116 (17.2)	2,936 (0.4)	2,930 (0.4)	4,281 (0.5)
₹10	12,222 (25.0)	18,536 (32.8)	21,288 (33.0)	12,222 (1.8)	18,536 (2.4)	21,288 (2.3)
₹20	2,200 (4.5)	2,341 (4.1)	3,020 (4.7)	4,399 (0.6)	4,681 (0.6)	6,040 (0.7)
₹50	4,888 (10.0)	4,211 (7.4)	3,196 (5.0)	24,440 (3.6)	21,057 (2.7)	15,980 (1.7)
₹100	13,702 (28.0)	13,836 (24.5)	14,024 (21.7)	1,37,028 (20.1)	1,38,364 (17.6)	1,40,243 (15.0)
₹500	6,166 (12.6)	7,290 (12.9)	8,906 (13.8)	3,08,304 (45.3)	3,64,479 (46.2)	4,45,311 (47.6)
₹1,000	1,918 (3.9)	2,383 (4.2)	3,027 (4.7)	1,91,784 (28.2)	2,38,252 (30.2)	3,02,713 (32.4)
<b>Total</b>	<b>48,963</b>	<b>56,549</b>	<b>64,577</b>	<b>6,81,133</b>	<b>7,88,299</b>	<b>9,35,856</b>

**Note:** Figures in parentheses represent percentage share in total.

Source Annual Report of RBI – 2010-11

TABLE-D1

**Alternative Estimates of Black Income**  
**(As per cent of GNP or GDP)**

Year	Chopra's estimates		Gupta & Gupta's estimates	Gupta & Mehta's estimates	Ghosh et.al's estimates	Rangnekar's estimates
	"Wanchoo method"	"Own Method"				
(1)	(2)	(3)	(4)	(5)	(6)	(7)
1970-71	4.8	5.2	22.3	--	7.6	--
1971-72	5.1	3.2	28.7	--	7.8	--
1972-73	4.0	3.8	31.9	--	7.8	--
1973-74	4.9	8.1	27.1	--	7.4	9.9
1974-75	5.9	12.4	20.9	13.8	8.1	9.3
1975-76	5.6	9.9	25.0	--	8.4	10.0
1976-77	5.7	10.2	37.6	--	8.7	11.3
1977-78	--	--	38.4	--	8.7	12.1
1978-79	--	--	48.1	19.8	--	13.5
1979-80	--	--	--	--	--	14.4

*Source: Aspects of the Black Economy in India – Shankar Acharya (NIPFP)*

**TABLE-D2**  
**Size of the Shadow Economy in 28 Asian Countries**

<b>Shadow Economy (in % of official GDP) using DYMIMIC and Currency demand method</b>				
<b>Country</b>		<b>1999-2000</b>	<b>2001-02</b>	<b>2002-03</b>
1	Bangladesh	35.6	36.5	37.7
2	Bhutan	29.4	30.5	31.7
3	Cambodia	50.1	51.3	52.4
4	Hong Kong	16.6	17.1	17.2
5	<b>India</b>	<b>23.1</b>	<b>24.2</b>	<b>25.2</b>
6	Indonesia	19.4	21.8	22.9
7	Iran	18.4	19.4	19.9
8	Israel	21.9	22.8	23.9
9	Jordan	19.4	20.5	21.6
10	Korea	27.5	28.1	28.8
11	Kuwait	20.1	20.7	21.6
12	Lebanon	34.1	35.6	36.2
13	Malaysia	31.1	31.6	32.2
14	Mongolia	18.4	19.6	20.4
15	Nepal	38.4	39.4	40.8
16	Oman	18.9	19.4	19.8
17	Pakistan	36.8	37.9	38.7
18	Papua New Guinea	36.1	37.3	38.6
19	Philippine	43.4	44.5	45.6
20	Saudi Arabia	18.4	19.1	19.7
21	Singapore	13.1	13.4	13.7
22	Sri Lanka	44.6	45.9	47.2
23	Syria	19.3	20.4	21.6
24	Taiwan	25.4	26.6	27.7
25	Thailand	52.6	53.4	54.1
26	Turkey	32.1	33.2	34.3
27	U.A.E.	26.4	27.1	27.8
28	Yemen Republic	27.4	28.4	29.1
	<b>Average</b>	<b>28.5</b>	<b>29.5</b>	<b>30.4</b>

TABLE-E1

## List of DTAA countries as in 2009 (78)

Sl. No.	Country with which India has DTAA	Whether under renegotiation	Sl. No.	Country with which India has DTAA	Whether under renegotiation
1	Armenia	Yes	40	Morocco	Yes
2	Australia	Yes	41	Myanmar*	
3	Austria	Yes	42	Namibia	Yes
4	Bangladesh	Yes	43	Nepal	Yes
5	Belarus	Yes	44	Netherlands	Yes
6	Belgium	Yes	45	New Zealand	Yes
7	Botswana	Yes	46	Norway	Yes
8	Brazil	Yes	47	Oman	Yes
9	Bulgaria	Yes	48	Philippines	Yes
10	Canada	Yes	49	Poland	Yes
11	China	Yes	50	Portuguese Republic	Yes
12	Cyprus	Yes	51	Qatar	Yes
13	Czech Republic	Yes	52	Romania	Yes
14	Denmark	Yes	53	Russia	Yes
15	Egypt	Yes	54	Saudi Arabia	Yes
16	Finland	Yes	55	Serbia	Yes
17	France	Yes	56	Singapore	Yes
18	Germany	Yes	57	Slovenia	Yes
19	Greece	Yes	58	South Africa	Yes
20	Hungary	Yes	59	Spain	Yes
21	Iceland*		60	Sri Lanka	Yes
22	Indonesia	Yes	61	Sudan	Yes
23	Ireland	Yes	62	Sweden	Yes
24	Israel	Yes	63	Swiss Confederation	Yes
25	Italy	Yes	64	Syria	Yes
26	Japan	Yes	65	Tajikistan*	
27	Jordan	Yes	66	Tanzania	Yes
28	Kazakhstan	Yes	67	Thailand	Yes
29	Kenya	Yes	68	Trinidad and Tobago	Yes
30	Korea	Yes	69	Turkey	Yes
31	Kuwait	Yes	70	Turkmenistan	Yes
32	Kyrgyz Republic	Yes	71	UAE	Yes
33	Libya	Yes	72	Uganda	Yes
34	Luxembourg	Yes	73	UK	Yes
35	Malaysia	Yes	74	Ukraine	Yes
36	Malta	Yes	75	USA	Yes
37	Mauritius	Yes	76	Uzbekistan	Yes
38	Mongolia	Yes	77	Vietnam	Yes
39	Montenegro	Yes	78	Zambia	Yes

\* The three countries, i.e. Iceland, Tajikistan and Myanmar already have the specific provision and hence, remaining 75 countries were taken up for renegotiation.

TABLE-E2

**A. Status of old DTAA's**

<b>No of countries with whom DTAA's were in force in 2009.</b>	<b>No of countries with whom we are negotiating article allowing for exchange of banking information along with names</b>	<b>No of countries with whom these renegotiations are finalized and signed along with names</b>	<b>No of the countries with which revised agreement signed and entered into force</b>
<b>Total 78</b> (see the list attached). Out of these, 3 DTAA's already had specific provision for exchange of banking information	<b>Total 75</b> (In the list of 78 countries, three countries, i.e. Iceland, Tajikistan and Myanmar already have the specific provision and hence, remaining 75 countries were taken up for renegotiation)	<b>Negotiation finalized: 28</b> Armenia, Australia, Bangladesh, Brazil, Finland, France, Indonesia, Kenya, Luxembourg, Malaysia, Malta, Morocco, Nepal, Netherlands, Norway, Romania, Singapore, Sri Lanka, South Africa, Spain, Sweden, Switzerland, Tanzania, Thailand, United Kingdom, UAE, Uzbekistan, Zambia	<b>Signed (7):</b> Australia, Finland, Nepal, Norway, Singapore, Switzerland and Tanzania <b>Entered into force(5):</b> Finland, Luxembourg, Singapore, Switzerland and Tanzania

**B. Status of New DTAA's since 2009**

<b>No of countries with whom negotiation for new DTAA's have been completed</b>	<b>No of new DTAA's signed</b>	<b>No of new DTAA's entered into force</b>
<b>Total 19</b> Albania, Bhutan, Chile, Croatia, Colombia, Estonia, Ethiopia, Fiji Georgia, Hong Kong, Iran, Latvia, Lithuania, Mexico, Mozambique, Senegal, Taiwan, Uruguay, Venezuela,	<b>Signed(9):</b> Colombia, Ethiopia, Georgia, Mexico, Mozambique, Lithuania, Taiwan, Uruguay, Estonia	<b>Entered into force(4):</b> Georgia, Mexico, Mozambique, Taiwan

**C. Total DTAA's in force as on date**

**82 DTAA's - 78 above plus four more new DTAA's (with Georgia, Mexico, Mozambique and Taiwan)**

TABLE-E3

## STATUS OF TAX INFORMATION EXCHANGE AGREEMENTS

No of countries with whom TIEAs are being negotiated along with names	No of countries with whom TIEA negotiations are finalised along with names	No of countries with whom TIEA have been signed along with names
<b>Total 22</b> ( Argentina, Bahrain, Bermuda, Bahamas, British Virgin Islands, Cayman Islands, Congo, Costa Rica, Gibraltar, Guernsey, Isle of Man, Jersey, Liberia, Liechtenstein, Macau, Maldives, Marshall Islands, Monaco, Netherland Antilles, Panama, Saint Kitts & Nevis, Seychelles)	<b>Total 17</b> (Argentina, Bahamas, Bahrain, Bermuda, British Virgin Islands, Cayman Islands, Congo, Costa Rica, Gibraltar, Guernsey, Isle of Man, Jersey, Liberia, Macau, Marshall Islands, Monaco, Saint Kitts & Nevis)	<b>Signed (10):</b> Argentina, Bahamas, Bermuda, British Virgin Islands, Cayman Islands, Guernsey, Isle of Man, Jersey, Liberia and Macua  <b>Entered into force(5):</b> Bahamas, Bermuda, British Virgin Islands, Cayman Islands and Isle of Man

TABLE-F1

Act	Section	Offence	Maximum	Minimum
NDPS Act 1985	15	Punishment for contravention in relation to poppy straw	Small quantity - up to 6 months or fine up to Rs. 10,000 or both. More than small quantity but less than commercial quantity - up to 10 years + fine up to Rs. 1 Lakh. Commercial quantity - 10 to 20 years + fine Rs. 1 to 2 Lakhs	
	18(c), 20, 16	Cultivation of opium, cannabis or coca plants without licence	Rigorous imprisonment-up to 10 years + fine up to Rs.1 lakh	
	19	Embezzlement of opium by licensed farmer	Rigorous imprisonment -10 to 20 years + fine Rs. 1 to 2 lakhs	
	17, 18, 20, 21 and 22	Production, manufacture, possession, sale, purchase, transport, import / export inter-state or use of narcotic drugs and psychotropic substances	Small - up to 6 months or fine up to Rs. 10,000 or both. More than small - up to 10 years + fine up to Rs. 1 Lakh. Commercial quantity - Rigorous imprisonment 10 to 20 years + fine Rs. 1 to 2 Lakhs	
	23	Import, export or transshipment of narcotic drugs and psychotropic substances	Small - up to 6 months or fine up to Rs. 10,000 or both. More than small - up to 10 years + fine up to Rs. 1 Lakh. Commercial quantity - 10 to 20 years + fine Rs. 1 to 2 Lakhs	
	24	External dealings in NDPS	10 to 20 years + fine of Rs. 1 to 2 lakhs	
	25	Knowingly allowing one's premises to be used for committing an offence	Same as for the offence	
	25A	Violations pertaining to controlled substances	Up to 10 years + fine Rs. 1 to 2 lakhs	
	27A	Financing traffic and harbouring offenders	10 to 20 years + fine Rs. 1 to 2 lakhs	
	28; 29	Attempts, abetment and criminal conspiracy	Same as for the offence	
	30	Preparation to commit offence	Half the punishment for the offence	
	31; 31A	Repeat offence	One and half times. Death penalty in some cases.	
	27, 64A	Consumption of drugs; Immunity	Cocaine, morphine, heroin - up to 1 year or fine up to Rs. 20,000 or both. Other drugs - up to 6 months or fine up to Rs. 10,000 or both.	
	32	Punishment for violations not elsewhere specified	Imprisonment up to six months or fine or both	

Act	Section	Offence	Maximum	Minimum
Customs Act 1962	132	False declaration, false documents, etc	Up to two years, or with fine, or with both.	
	133	Obstruction of officer of customs	Up to two years, or with fine, or with both.	
	134	Refusal to be X-Rayed	Up to six months, or with fine, or with both	
	135	Evasion of duty or prohibitions	Up to seven years and with fine	1 year
	136	Offences by officers of customs	Up to three years, or with fine, or with both	
Central Excise Act 1944	9	Evasion of duty	Up to seven years and with fine	3 years or with fine or with both
PMLA 2002	4	Punishment for Money-Laundering	7 years with fine up to Rs.5 lakhs	3 years
		Offence in Para 2 Part A of Schedule	10 years with fine up to Rs.5 lakhs	3 years
PC Act 1988	7	Public servant taking gratification other than legal remuneration in respect of an official act	Up to five years and fine	6 months
	8	Taking gratification, in order, by corrupt or illegal means, to influence public servant	Up to five years and fine	6 months
	9	Taking gratification, for exercise of personal influence with public servant	Up to five years and fine	6 months
	10	Punishment for abetment by public servant of offences defined in section 8 or 9	Up to five years and fine	6 months
	11	Public servant obtaining valuable thing, without consideration from person concerned in proceeding or business transacted by such public servant	Up to five years and fine	6 months
	12	Punishment for abetment of offences defined in section 7 or 11	Up to five years and fine	6 months
	13	Criminal misconduct by a public servant	Up to seven years and fine	1 year
	14	Habitual committing of offence under section 8, 9 and 12	Up to seven years and fine	2 years
	15	Punishment for attempt	Up to three years and fine	



TABLE-F2

**Existing and proposed minimum and maximum punishments  
under economic laws**

		PRESENT IMPRISONMENT			PROPOSED	
		Maximum	Minimum	Death	Maximum	Minimum
1	Income Tax Act	7	0		7	3 months
2	Wealth Tax Act	7	0		7	3 months
3	Customs Act	7	0		7	3 months
4	Central Excise Act	7	0		7	3 months
5	P C Act	7	0		10	6 months
6	PML Act	10	3		No change	No change
7	NDPS Act	20	0	Yes*	Life Imprisonment	6 months

**NOTES**

\* For second conviction punishable with 10-20 years imprisonment.

1. Imprisonment is in years, unless otherwise mentioned.

2. There should be no provision of death sentence for economic offences.

**ANNEX-G1****Proposed amendments in the tax law introduced in the Finance Bill 2012 aimed at curbing tax evasion and reducing black economy –**

- (i) Unexplained cash credits / investments / expenditure, etc., under section 68, 69, 69A, 69B, 69C and 69D – **Part I, Chapter VI, Para 6; Part II, Page 9, Para 3.42**
- (ii) Compulsory filing of income tax return in relation to assets located outside India – **Part II, Page 19, Para 12.8**
- (iii) Reassessment of income in relation to any asset located outside India – **Part I, Chapter VI, Para 6.48; Part II, Page 19, Para 12.4**
- (iv) Penalty on undisclosed income found during the course of search – **Part I, Chapter VI, Para 6**
- (v) Expediting prosecution proceedings under the Act – **Part I, Chapter VI, Para 6.44**
- (vi) Definition of Commissioner to include Director – **Part II, Page 8, Para 3.40**
- (vii) Prohibition of cash donations in excess of ten thousand rupees – **Part I, Chapter III, Para 3.42; Part II, Page 5, Para 3.16**
- (viii) Share premium in excess of the fair market value to be treated as income – **Part II, Page 6, Para 3.24**
- (ix) Tax Collection at Source (TCS) on cash sale of bullion and jewellery - **Part I, Chapter VI, Para 6.21**
- (x) Income deemed to accrue or arise in India – **Part II, Page 20-21, Para 12.10.3 & 12.10.4**
- (xi) Taxation of a non-resident entertainer, sports person etc. – **Part II, Page 19, Para 12.6**
- (xii) Tax Residence Certificate (TRC) for claiming relief under DTAA – **Part II, Page 21, Para 12.10.4**
- (xiii) Extension of time limit for completion of assessment or reassessment where information is sought under a DTAA – **Part I, Chapter VI, Para 6.48; Part II Page 19, Para 12.5**
- (xiv) Advance Pricing Agreement (APA) – **Part II, Page 18, Para 12.2**
- (xv) Filing of return of income, definition of international transaction, tolerance band for ALP, penalties and reassessment in transfer pricing cases – **Part I, Chapter VI, Para 6**
- (xvi) General Anti-Avoidance Rules (GAAR) – **Part II, Page 18, Para 12.3**
- (xvii) Customs duty on gold import enhanced from 2% to 4% – **Part I, Chapter VI, Para 6.20**

## **ANNEX-G2**

### **LIST OF PAST CHAIR / CO-CHAIR & MEMBERS OF THE COMMITTEE**

#### **CHAIR**

SHRI SUDHIR CHANDRA, CBDT

SHRI PRAKASH CHANDRA, CBDT

SHRI MUKESH CHAND JOSHI, CBDT

#### **CO-CHAIR**

SHRI SATYENDRA SINGH RANA, CBDT

#### **MEMBERS**

SHRI ARUN MATHUR, ED

SHRI AMITABH RAJAN, ED

SHRI RAKESH SINGH, ED

SHRI R K SRIVASTAVA, MOL

SMT SHARDA JAIN, MOL

## ABBREVIATIONS USED

**ASSOCHAM** The Associated Chambers of Commerce and Industry of India

**AG** Accountant General

**AS** Accounting Standards

**BRICS** Brazil, Russia, India, China & South Africa

**C&AG** Comptroller and Auditor General of India

**CBDT** Central Board of Direct Taxes

**CBEC** Central Board of Excise & Customs

**CBI** Central Bureau of Investigation

**CEIB** Central Economic Intelligence Bureau

**CENVAT** Central value Added Tax

**CIB** Central Information Branch

**COIN** Customs Overseas Intelligence Network

**CPC** Civil Procedure Code

**Cr PC** Criminal Procedure Code

**CTR** Cash Transactions Report

**CVC** Central Vigilance Commission

**DARTTS** Data Analysis & Research for Trade Transparency System

**DCI** Directorate of Criminal Investigation

**DEPB** Duty Entitlement Pass Book

**DFIA** Duty Free Import Authorization

**DGCEI** Directorate General of Central Excise Intelligence

**DGIT** Director General of Income Tax

**DRI** Directorate of Revenue Intelligence

**DoC** Directorate of Currency

**DYMIMIC** Dynamic-Multiple Indicators Multiple-Causes

**ED** Directorate of Enforcement

**EIC** Economic Intelligence Council

**FATF** Financial Action Task Force

**FCRA** Foreign Contribution Regulation Act

**FEMA** Foreign Exchange Management Act

**FICCI** Federation of Indian Chambers of Commerce and Industry

**FICN** Fake Indian Currency Note

**FII** Foreign Institutional Investor

**FINnet** Financial Intelligence Network

**FIU-IND** Financial Intelligence Unit- India

**FLETC** Federal Law Enforcement Training Center

**FMC** Forward Market Commission

**FRBM** Fiscal Responsibility and Budget Management Act

**FTA** Free Trade Agreements

**FT&TR** Foreign Tax & Tax Research

## ABBREVIATIONS USED

<b>ICAI</b>	Institute of Chartered Accountants of India
<b>IRDA</b>	Insurance Regulatory and Development Authority
<b>IPC</b>	Indian Penal Code
<b>GDP</b>	Gross Domestic Product
<b>GST</b>	Goods and Service Tax
<b>HQ</b>	Head Quarter
<b>HSN</b>	Harmonized System of Nomenclature
<b>KYC</b>	Know Your Customer
<b>L&amp;C</b>	Legislation & Computerization
<b>MHA</b>	Ministry of Home Affairs
<b>MLAT</b>	Mutual Legal Assistance Treaties
<b>MGNREGS</b>	Mahatma Gandhi National Rural Employment Guarantee Scheme
<b>NAS</b>	National Accounting System
<b>NCAER</b>	National Council of Applied Economic Research
<b>NCB</b>	Narcotics Control Bureau
<b>NDPS</b>	Narcotic Drugs and Psychotropic Substances Act
<b>NIFM</b>	National Institute of Financial Management
<b>NIPFP</b>	National Institute of Public Finance and Policy
<b>NOC</b>	No Objection Certificate
<b>NPO</b>	Non-Profit Organisation
<b>PAN</b>	Permanent Account Number
<b>PMLA</b>	Prevention of Money Laundering Act
<b>PN</b>	Participatory Note
<b>PTA</b>	Preferential Trade Agreements
<b>RBI</b>	Reserve Bank of India
<b>RI</b>	Rigorous Imprisonment
<b>SEBI</b>	Securities and Exchange Board of India
<b>SFIO</b>	Serious Frauds Investigating Office
<b>STR</b>	Suspicious Transactions Report
<b>TBML</b>	Trade Based Money Laundering
<b>TIEA</b>	Tax Information Exchange Agreements
<b>TRAI</b>	Telecom Regulatory Authority of India
<b>TTU</b>	Trade Transparency Unit
<b>UID</b>	Unique Identity
<b>UNCAC</b>	United Nations Convention Against Corruption
<b>URD</b>	Un-registered dealers
<b>VAT</b>	Value Added Tax
<b>VKGUY</b>	Vishesh Krishi Gram Upaj Yojana
<b>WGC</b>	World Gold Council