

## Towards a Clean and Transparent Economy

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*A prosperous ruler will govern the state well, take up welfare activities for the people and promote commercial activities with the result that soon the people will also become prosperous - Chanakya*



***Black money generated through tax evasion is an economic challenge as well as a social menace. ... Government has taken a slew of measures, almost amounting to waging of war against black money, in the past three years. These involve policy-level reforms through legislative and administrative initiatives, effective enforcement, capacity building, and building intelligence through data mining***

**I**ndia continues to remain very low in the UN's Human Development Index with the poor and needy largely remaining so. Last year (HDI-2016), it was ranked a poor 131 among 188 countries.

Serious efforts have, however, been made to take the reforms to the next level, with the goal of benefitting those who were so far in the fringes of economic growth. The main pillars of this strategy are inclusion, transparency and decentralisation. The efficient implementation of these three pillars, would, for the first time, take the benefits of growth directly to the people. Of these three segments, perhaps, transparency is the most important prerequisite for secular economic growth. Dispassionate examination will point at corruption as the main culprit that failed every well intentioned programme. Corruption breeds black money and together they subvert welfare programmes, restrict the flow of finance to the government, constricting its ability to formulate and implement programmes and discourage foreign investment that brings money and technology for economic development, generating job opportunities in a nation struggling to give employment avenues to its young population.

According to the World Bank, corruption is public enemy number one in the developing world and the poor pay the highest percentage of their income in bribes. India has been no exception. Interestingly, government, while mounting a frontal attack on black money hoarders, has simultaneously initiated steps for insulating the poor from corruption and bribery by innovating delivery systems. Some of the key initiatives are discussed in this article.

### **Towards a Clean Economy:**

India's tax to GDP ratio is a mere 16.6 per cent, with a tax base of around 5.5 crore persons which includes companies, individuals and other business forms. As per the Economic Survey 2016-17, India has only 7 taxpayers for every 100 voters. This tax evasion is glaring from the fact that while more than 1.25 crore cars were sold in the last five years and more than 2 crore individuals travelled abroad in 2015 alone, mere 1.72 lakhs individuals reported income more than Rs.50 lakh for tax purposes.

Black money generated through tax evasion is an economic challenge as well as a social menace. While it harbours bribery, electoral corruption, organized crimes and ostentatious consumption it distorts economic planning and financial integrity of the

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nation. On the whole it deepens the economic inequality and corrodes the social fabric of the nation. Government has taken a slew of measures, almost amounting to waging of war against black money, in the past three years. These involve policy-level reforms through legislative and administrative initiatives, effective enforcement, capacity building, and building intelligence through data mining.

### Tax Administration for a Clean Economy

Following path breaking measures have been taken to address the menace of black money:

- ❖ Special Investigation Team (SIT)—headed by former SC judge M.B.Shah was formed to probe black money.
- ❖ ‘The Black Money (Undisclosed Foreign Income and Assets) and Imposition of Tax Act, 2015’ with stringent penal provisions including rigorous imprisonment of 3-10 years has been enacted to effectively deal with the issue of black money stashed away abroad. Tax evasion has been made a predicate offence, under Prevention of Money Laundering Act (PMLA).
- ❖ Rs 8,186 crore, illegally kept in offshore banks by Indians, has been brought under tax ambit despite several constraints.
- ❖ Multi-Agency Group (MAG) was set up for facilitating coordinated and speedy investigation of cases of Panama Papers leaks.
- ❖ Signing Double Taxation Avoidance Agreements (DTAAs)/ Tax Information Exchange Agreements (TIEAs)/Multilateral Conventions etc. with other nations.
- ❖ Joining Multilateral Competent Authority Agreement in respect of Automatic Exchange of Information to support global efforts against black money.

- ❖ Signing information sharing arrangement with USA under its Foreign Account Tax Compliance Act (FATCA).

- ❖ Renegotiation of DTA with Mauritius, Singapore and Cyprus to curb treaty abuse, tax evasion and round-tripping of funds.

- ❖ Though Participatory Notes (PN) bring foreign investment, but they have been red flagged as a conduit to route black money back into the country by SIT on black money. SEBI mandated increased disclosure requirements and restricted transfer of PN to curb money laundering in order to keep track of their beneficial owners.

- ❖ Enactment of Benami Transactions (Prohibition) Amendment Act, 2016’ which empowers the government to confiscate benami properties—assets (without any compensation) held in the name of another person or under a fictitious name. The act has a provision for imprisonment up to seven years. As per Department of Revenue, more than 245 benami transactions have already been identified and provisional attachments of properties worth Rs.55 crore have been made in 124 cases.

- ❖ 23064 searches / surveys have been conducted (Income Tax 17525; Customs 2509; Central Excise 1913; Service Tax 1120) to detect tax-evasion of more than Rs. 1.37 lakh crore (Income Tax 69434; Customs 11405; Central Excise 13952; Service Tax 42727).

- ❖ Launching prosecutions in 2814 cases leading to arrest of 3893 persons.

- ❖ ED registered 519 cases and conducted 396 searches leading to



arrests in 79 cases and attachment of properties worth Rs.14,933 crore.

- ❖ 64,275 declarants made disclosures of Rs 65,250 crores under the Income Declaration Scheme (IDS), 2016 which provided a chance to domestic black money holders to come clean.

### Budget 2017-18 – ‘Transform, Energise and Clean India’

Taking forward the crusade against black money they Finance Minister proposed the following major reforms:

- ❖ Cash expenditure upto Rs 10,000/- only is allowed as deduction to businesses.
- ❖ Charitable trusts can receive cash donations up to Rs 2,000 only from a single source.
- ❖ Restricting cash expense to Rs 2 lakhs only for a single transaction and in case of violation a penalty of equal amount would be levied.
- ❖ Primary Agriculture Credit Societies which are susceptible to misuse by parking black money, are to be computerized and integrated with the Core Banking System of District Central Cooperative Banks.
- ❖ Exemption from long-term capital gains tax has been restricted to shares on purchase of which Securities Transaction Tax has been paid (and other “genuine cases” such as public offers). This

will clamp down on tax evasion through "sham transactions"

- ❖ Proposed legislation, to confiscate the assets located within the country, of the offenders, including economic offenders, who fled from the country till they submit themselves to law of the land.
- ❖ Aadhaar has been made mandatory for filing of income-tax returns as well as for obtaining and retaining the PAN. This would solve the problem of multiple and bogus PAN and strengthen KYC verification for different transactions including opening of bank account.

#### ❖ **Rewarding Honest Taxpayers**

While the government aims to increase the tax base, it is striving to build a predictable and stable taxation regime so as to be investor friendly and growth spurring. Following are some of the noteworthy initiatives/policy changes towards better tax administration:

- ❖ Without forgoing its sovereign right to undertake retrospective legislation, government has made it very clear that it would exercise this with extreme caution and judiciousness.
- ❖ E-assessment has been launched in 7 cities in order to reduce physical interface between tax payer and the department along with cost and time of compliance.
- ❖ 'E-Sahyog' launched in 2015 to provide an online mechanism to resolve mismatches in Income-tax returns of those taxpayers whose returns have been selected for scrutiny to be expanded to reduce compliance cost, especially for small taxpayers.
- ❖ CBDT and CBEC to issue periodic clarifications on tax laws, on the recommendations of a High Level Committee setup to interact with trade and industry
- ❖ Resident taxpayers can also obtain an advance ruling in respect of

their income tax liability above a defined threshold.

- ❖ Scope of the Income-tax Settlement Commission has been enlarged so that more taxpayers can avail this opportunity.
- ❖ Time bound grievance redressal through PMO monitored 'Centralized Public Grievance Redress and Monitoring System (CPGRAMS)' and 'e-nivaran' portal.
- ❖ One page ITR form 'Sahaj' for select taxpayers.
- ❖ Income tax Department is working on the 'Project Insight' to strengthen non-intrusive information-driven approach for improving tax compliance and speedy investigation.

#### **Demonetisation**

Demonetisation of high denomination currency of Rs 500 and Rs 1000 led to a regime shift by punitively raising the costs of tax evasion and striking at the roots of corruption. It was also aimed at countering fake currencies, greater digitalisation of the economy, increased flow of financial savings, and greater formalization of the economy, all of which could eventually lead to higher GDP growth, better tax compliance and greater tax revenues.

Post demonetisation, almost all cash has entered the banking system providing scope to the law enforcement agencies to keep track of the money trail. Investigation of cash deposits have uncovered various fraudulent practices including back dating of sales, benami deposits, sale of jewellery, bullion, luxury goods and forex to unidentified persons (without PAN), splitting of bills to avoid reporting of PAN, depositing in cooperative banks (which do not have stringent KYC norms), deposits in multiple accounts against single PAN; etc.

Data have shown that deposits between Rs 2 lakh and Rs 80 lakh, totalling to Rs 5.48 lakh crore were made during demonetisation, in 1.09

crore accounts. A total of Rs 4.89 lakh crore, comprising deposits of over Rs 80 lakh, entered into 1.48 lakh accounts. As part of *Operation Clean Money*, the department of income tax sent e-mails and text messages to 18 lakh individuals in the first phase. Response from 12 lakh accounts have been received on the department's e-filing website. This would help the department to eliminate genuine cases from further investigation. In a written reply to the Rajya Sabha, the Finance Minister stated that the Income Tax Department has seized cash and valuables totalling Rs 600 crore in 1100 searches and survey operations conducted post demonetisation.

Giving a chance to come clean, Government announced Pradhan Mantri Garib Kalyan Yojana under which those who declared cash deposits, (till 31<sup>st</sup> March, 2017) could pay a tax of 50 per cent and deposit 25 per cent of the amount declared into the noninterest-bearing PMGK Deposit Scheme for four years. There is no official data yet on the PMGKY. Irrespective of the numbers, it is important that a frame work was provided to common people to regularise the cash which they had come to possess unwittingly.

#### **Digital Economy**

The predominance of cash in the economy is the major reason of large scale tax evasion. According to a 2015 report from PwC, 98 percent of all transactions by volume and 68 percent of the total value of transactions are conducted in cash in India. Demonetisation has given a quantum push to digital transactions. While the advantages of digital economy are many, it inter alia creates transparency. Top ranking countries in the Corruption Perception Index of Transparency International have reported less than 10 per cent of the total transaction in cash. India stands at a distant 79<sup>th</sup> position in this ranking.

The National Payments Corporation of India has successfully implemented the Unified Payments

Interface platform which facilitates inter-operability; BHIM (196 lakh people have downloaded it) and Aadhaar Pay will facilitate peer-to-peer transactions and digital payments over the counter respectively. Green shoots of long term benefits are already seen in the RBI data which shows that UPI based transactions jumped 20 per cent to Rs 2000 crore in March'17.

In order to incentivise digital transactions, presumptive rate of income tax for non-cash transactions of small and medium tax payers with turnover up to Rs 2 crores has been brought down from 8 per cent to 6 per cent. Further, government has exempted BCD, Excise/CV duty and SAD on POS machines and micro ATMs.

While the government has mandated the linking of PAN with Aadhaar, as a further step it may consider compulsory Aadhaar authentication for cash transactions beyond Rs 50,000/-.

### Goods and Services Tax (GST)

GST, one of the biggest tax reforms post-independence is aimed at simplifying the complicated indirect tax regime. It will create a common Indian market, streamline tax administration, improve tax compliance, boost investment and growth and result in higher revenue collection; by subsuming all indirect taxes (other than custom duty) levied by the Central and state governments. With the passing of four bills related to GST in the Parliament, GST came a step closer to meet its July 1<sup>st</sup> target of rollout. With a state of art GST information technology architecture and provision for stringent penalties and prosecution for tax evasion, India may see a surge in tax to GDP ratio in medium to long term. Further, correct reporting of business transactions would automatically lead to buoyancy in the direct tax collection.

### Electoral Funding Reforms

Political parties received Rs 7,833 crore funding from unknown sources between 2004-05 and 2014-15, which



is 69 per cent of their total income, as per the report of the think tank, Association of Democratic Reforms, leaving us to guess the unknown sources. Political funding by industrial and business houses, when shrouded in secrecy, is the breeding ground for vested interests. It nourishes the unholy nexus between politics and business, forcing the politician to return the favours, subverting democracy and people's will. Thus, transparency in political funding is essential for clean economy.

A small beginning has been made in the budget 2017 by limiting of cash donations to political parties from a single source to Rs. 2,000. The concept of electoral bond has been proposed whereby corporate donations will be kept anonymous safeguarding the interest of the donor but the source can be traced.

### Bypassing Corruption

Since independence, welfare schemes have proliferated with the aim of taking the fruits of development to the poor and the needy. However, the malaise of corruption has spread over the years throughout these schemes resulting in massive leakages and lining the pockets of the undeserving. The Economic Survey for FY 2015-16, for instance revealed that 40-50 per cent of the benefits under the flagship scheme of PDS are lost due to leakages. The government has used an innovative mechanism namely Direct Benefit Transfer (DBT), to transfer the

money value of the benefits directly into the accounts of the deserving poor, bypassing corruption. A massive drive was launched in 2014 to take banking to the poor and under privileged, on which the structure of DBT is being erected. The trinity of Jan-Dhan (around 25.7 crore accounts opened), Aadhaar (crossed 112 crore enrolment) and Mobile has provided the foundation for transparency and inclusiveness. It has been reported that presently, 84 schemes in 17 ministries are covered under the DBT saving 50,000 crores over the last three years. Uploading the list of beneficiaries for anyone to verify could be the next step to bring further transparency.

Government has also streamlined and removed scope for grand corruption by mandating auction as the only route for allocation of natural resources, through amendment of Mines and Minerals (Development and Regulation) act and by launching Government eMarketplace (GeM) for procurement of goods and services by the Government Ministries/ Departments, PSUs, and autonomous bodies. Such measures attack the source of corruption and augment resources for nation building activities.

### Unfinished Agenda

While applauding the courage and conviction of the government for the creation of a 'Clean India', following further steps are required for a sustained and systemic solution, which are illustrative but not exhaustive.

- ❖ Simplification of tax laws and procedures is *sine qua non* for an effective and corruption free tax administration. It should leave least scope for discretion and litigation. It was revealed in the budget speech of 2016-17 that 3 lakh tax cases are pending before the 1st Appellate Authority with disputed amount being 5.5 lakh crores.
- ❖ Prevention of misuse of legal persons is another area that requires strengthening. Shell companies have mushroomed over a period of time abusing the simplified corporate procedures. Hundreds of companies are registered in a single address. Typically they have low capital, single or no employee and directors who are men of no means. Over the years such shell companies have established a well-oiled system of producing fake bills, providing bogus share capital, bogus loan and for that matter they are used for faking any financial transaction. They are hard to detect because of the sheer numbers and when detected hard to prove under the existing evidentiary standards. During the period 2013-14 to 2015-16, IT investigations led to detection of more than 1,155 shell companies / entities used as conduits by over 22,000 beneficiaries involving non-genuine transactions of more than Rs. 13,300 crore. However, there have been mixed results before the courts of appeal in the cases filed against these companies. It would do well to think in the direction of defining such offences as running a shell company and faking financial transactions as organised crime and enact a penal law to tackle the same.
- ❖ Reduce human interface between the tax men and the tax payers. Minimal interaction that is permitted should be standardised and amenable to oversight by higher authorities. E assessment initiated by the IT department is a step in the right direction.
- ❖ The Financial Action Task Force (FATF), in which India is a member, has recommended that nations should consider requiring their financial institutions to identify their business relationships with politically exposed persons (PEPs) (persons entrusted with a prominent public function) and put appropriate risk management system in place as a preventive measure.
- ❖ Promote seamless coordination among law enforcement agencies at the centre and the state level.

#### Sustained Effort Required

The bold steps taken by the Government to combat corruption and to clean the economy are showing appreciable results. If the campaign is pursued with equal vigour and imagination it will usher in an economic architecture spawning myriad benefits from the poor to the rich, removing poverty, creating employment for many and upgrading the much needed skills. The process cannot be without certain amount of pain which is inevitable in any transition. Nothing comes without sacrifice and in this case, too small a price to pay for a clean and transparent economy. □

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