DUMMY COMPANIES: ENTERPRISE FOR GENERATION OF BLACK MONEY

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ABSTRACT

The issues of generation of black money, its stashing abroad in tax havens and offshore financial Centre's have attracted public attention in past few years in India. There are various illegal and legal permissible economic activities for the generation of black money. The study has made an attempt to assess the generation of black money through companies, particularly in terms of who form these companies, what are the motives of formation of these dummy companies. The results indicate that some companies are an important source for the generation of black money. Many businessmen andp oliticians are involved in this phenomenon, by which they are generating black money or convert their black money into white money. It is the safest means of generation of black money. Various companies are registered but they are either not paying their return or not involve in any business transactions or doing illegal activities such include money laundering, billing schemes, fictitious service schemes, bankruptcy fraud, tax evasion, and market manipulation. The estimates of black money is very high and increasing year by year, this also leads to the growth of parallel economy, which has been expanding very rapidly in India as well as in developing countries.

Key Words: Black money, Company, Shell Company, Money Laundering,Tax evasion, Hawala Operator, India.

INTRODUCTION

Generation of black money has dominated discussions and debate in public for during the last few years. Members of Parliament, the Supreme Court of India and the public at large have unequivocally expressed concern on the issue, particularly after some reports suggested estimates of such unaccounted wealth being held abroad.Indian government is more concerned about the increasing amount of black money and prevalence of the parallel economy for which various commissions are formed for controlling but results are not so impressive. 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. Today issue of black money is become very important as it affects the whole economy of the country.

BLACK MONEY

Several terms are in use to define black money 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, 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 to evade payment of taxes (income tax, excise duty, sales tax, stamp duty, etc), to evade compliance with the provisions of industrial laws such as the Industrial Dispute Act1947, Minimum Wages Act 1948, Payment of Bonus Act 1936, Factories Act 1948, and Contract Labour (Regulation and Abolition) Act 1970 and other laws and administrative procedures and to evade payment of other statutory contributions. National Institute of Public Finance and Policy (NIPFP)defined black income as 'the aggregates of incomes which are taxable but not reported to the tax authorities'.

MONEY LAUNDERING

Money Laundering refers to the conversion or laundering of money which is illegallyobtained, so as to make it appear to originate from a legitimate source. Money Laundering is being employed by launderers worldwide to conceal criminal activity associated with it such as drug / arms trafficking, terrorism and extortion. Hiding or disguising the source of certain proceeds will of course, not amount to money laundering unless these proceeds were obtained from a criminal activity. Thus, Money Laundering is not an independent crime, it depends upon another crime(predicate offence), the proceeds of which is the subject matter of the crime in money laundering.

ESTIMATES OF BLACK MONEY IN INDIA

It is evident from the study that government of India introduced various commissions for estimating black money. Shri K.N. Wanchoo submitted a report in December 1971 on estimation of black money; he followed the method adopted by Prof. NicholasKaldor with some modifications. According to which black money was of amounting Rs.700 crore in 1961-62 which rose to Rs. 1000 crore in 1965-66.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 was estimated at 1800 crore.

Dr. D.K. Rangnekar, a member of the Wanchoo Committee, submitted his report in 1982, different from the estimates of Wanchoo Committee. According to him, tax-evaded income for 1961-62 was ofthe order of 1150 crore,2,350 crore in 1965-66. The projections for1968-69 and 1969-70 were 2833 crore and 3080 crore respectively.

The NIPFP conducted a study under the guidance of Dr. S. Acharyain 1985. He concluded that total black income generation Rs. 36,784 crore out of a total GDPat factor cost of 1,73,420 crore on the higher side. It was the last official study for estimating black money generation conducted by The Ministry of Finance.

As the issue of black money has become a dominated matter of discussion among public in last few years, the estimations again came into light. According to a report released by Global Financial Integrity (GFI) in December 2012, India is among the top 10 developing countries in the world with a black money outflow of USD 1.6 billion (Rs. 8,720 crore) in 2010. Total outflow of black money from India since independence until 2010 was USD 232 billion, generally in the form of corruption, bribery and kickbacks. The cumulative value of illicit assets held by Indians during the same period is estimated to be USD 487 billion.

GENERATION OF BLACK MONEY

There are three sources of black money – crime, corruption and business. The criminal componentof 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. The commercial component 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.

GENERATION OF BLACK MONEY IN COMPANIES

Studies correlating the use of company form of organization with the generation of huge amount of black money and the laundering of black money. Following are the various ways and means adopted by the companies for the generation of black money.

Manipulations inside the Organizations: Books of accounts are required to be maintained by every company under different laws, like the Companies Act 1956, the Banking Regulation Act, and the Income Tax Act. Companies manipulate their book of accounts by the suppression of receipts and inflation of expenditure for the generation of black money. Under-reporting of production figure is another means of artificiallyreducing tax liability. It may be resorted for the purpose of evading central excise, sales tax, or income tax. Suppression of closing stock or under valuation of inventories both in terms of quality and value is also a common method of understating profit.Companies may try to inflate expenses by obtaining bogus or inflated invoices from 'bill masters', who make bogusvouchers and charge nominal commission. Manipulation of capital expenses includesover-invoicing of plant and equipment or any other capital asset isan approach adopted to claim higher depreciation and thereby reduce the profit of the business.A company is required to pay taxes on profit or income which isthe difference between sale proceeds or receipts and expenditure. Thus manipulation of sales or receiptsis the easiest method of tax evasion. Thus, companies are generating huge amount of black money through different manipulations.

Hawala Operators: Companies transferred their illicit black income outside India and may come back to India through hawala operators. Number of more sophisticated versions of manipulation of expenses can also be resorted to bythose intending to generate black money, they are known as 'Hawala Operators'. These operatorsmay accept cheques for payments claimed as expense and return cash after charging some commission.There have been instances of claims of bogus expenses to foreign entities. The payments can be shownto foreign entities in the form of advertisement and marketing expenses or commission for purchases orsales. The funds may be remitted to the account of the foreign taxpayer and the money can either bewithdrawn in cash or remitted back to India in the form of non-taxable receipts. Such money may also beaccumulated in the form of unaccounted assets of the Indian taxpayer abroad.

Shell Companies: A shell company is an entity that has no active business and usually exists only inname as a vehicle for another company's business operations. In essence, shells arecorporations that exist mainly on paper, have no physical presence, employ no one andproduce nothing. They are frequently used to shield identities and/or to hide black money. Sometimes it can also involve hawala operators, who operateshell entities in the form of proprietorship firms, partnership firms, companies, and trusts.Shell companies are often associated with fraud. Although they are legal entitiesthat do have a legitimate function in business operations, shell companies are also utilizedby criminals to facilitate fraudulent activities. Such activities include money laundering,billing schemes, fictitious service schemes, bankruptcy fraud, tax evasion, and marketmanipulation. These companies are frequently linked to multiple forms of scams, law officials areunable to prosecute all cases because state agencies do not collect enough ownershipinformation on company formation documents. Thus, leaving no paper trail for thegovernment to trace back to a particular individual or individuals.

Trade Based Money Laundering (TBML): 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 moneythrough trade transactions. In practice, this can be achieved through the misrepresentation of the price, quantity or quality of imports or exports. Factors that facilitate such manipulation include the enormous volume of international trade flow, the complexity associated with financing arrangements and currency exchanges as well as limited recourse to verification procedures between countries.

External Trade and Transfer Pricing: More than 60 percent of global trade is carried out between associated enterprises of multinational enterprises (MNEs). Since allocation of costs and overheads and fixing of price of product/services are highly subjective, MNEs enjoy considerable discretion in allocating costs and prices to particular products/services and geographical jurisdictions. Such discretion enables them to transfer profit/income to no tax or low tax jurisdictions. Differing tax rates in different tax jurisdictions can create perverse incentives for corporations to shift taxable income from jurisdictions with relatively high tax rates to jurisdictions with relatively low tax rates as a means of minimising their tax liability.

Non Profit Organization (NPO): Taxation laws allow certain privileges and incentives for promoting charitable activities. Misuse of such benefits and manipulations through entities claimed to be constituted for nonprofit motive are among possible sources of generation of black money. Many businessmen and politicians are running these types of organizations for the motives of hiding and laundering their black money.

REAL LIFE EXAMPLES OF COMPANIES GENERATING BLACK MONEY

Prasant Bhushan, AamAadmi Party complained to SIT (Special Investigation Team) that the Indian High Commission in Singapore on 31 August 2011, had stated that Rs. 6,530 crore have come into India from Bio Metrix Marketing Ltd, a one room company in Singapore that does not do any business. It was a company with no assets, no equity and does not file an income tax returns in Singapore claiming to be a small company. Yet this company has invested Rs. 6,530 crore into India as foreign direct investment (FDI). The High Commission had also stated that all this money has gone into Reliance group companies in India with the major chunk going to Reliance Gas Transportation Infrastructure Ltd, which is a company 100% owned by Mr. MukeshAmbani personally. The Commission had pointed out that one Atul Shanti Kumar Dayal effectively owned this company Bio Metrix. Mr.Dayal is nothing but a front for Reliance, since he is a director in 32 Reliance group companies. Now it has come to light that this company Bio Metrix has closed down.

Congress leader Sonia Gandhi and Rahul Gandhiform a company called Young Indian with the deliberate intention of diverting funds from Associate Journals Ltd (AJL). AJL owns real estate properties worth millions in Delhi, Mumbai, Patna, Lucknow, Indore, Bhopal and other places. The metropolitan magistrate observed that it appears that Young India was in fact created as a sham or a cloak to convert public money to personal use or as a special purpose vehicle for acquiring control over Associated Journals Ltd assets worth over Rs 2,000 crore.

Alleged Hawala operator and Kanpur-based meat exporter MoinAkhtarQureshi has seen phenomenal growth in his wealth in the last decade. His meat export company AMQ Agro India, has posted a turnover of Rs 167 crore which, as per the IT department, is less than the actual wealth. He has started 25 companies since 1993, with AMQ Agro, which exports animal gut, being the flagship firm. Filings with the Registrar of Companies show that seven of his companies deal in real estate and have non-descript activities with a low paid-up capital base.Reports say that he is operating as ahawala operator and a money launderer too inside the veil of his business and misusing his company for the generation of black money.

CONCLUSION

Existence of black money has a significant impact on social, economic and political levels of ourlives.Indian economy is badly affected by black money as it is underestimating GDP,increasing inequality of income, increasing illegal activities etc. Such money is a new challenge for Indian economy as it affects the growth of the nation. Even after several decades of economic planning and push in the right direction, India still continues in the same state as an underdeveloped economy in terms of per capita income and the reason behind it is the existence loopholes in our tax laws, lack of tax morality, or non-compliant attitude of the citizenry towards tax laws.

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