

BLACK to WHITE MONEY***-TRADE RELATED MONEYLAUNDERING***

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Abstract: The generation of black money and its stashing abroad in tax havens and offshore financial centers have dominated discussions in India by the last year with the Cobrapost second sting operation which brought in to the public the money laundering activities of three private banks in India. Particularly some reports suggested estimates of such unaccounted wealth being held in abroad via clandestine channels. The objective of this paper is to place various dimensions of black money and its complex relationship with policy and governance in India .This also brings forth the framework, policy options, and the strategies that the Government of India has been pursuing to tackle this issue; especially recent initiatives and developments. This paper may be helpful in contributing to the current debate on the black money issue and help to develop a board consensus regarding the future course of action for it.

INTRODUCTION

“Sir, money, money, the most charming of all things; money, which will say more in one moment than the most elegant lover can in years. Perhaps you will say a man is not young; I answer he is rich. He is not genteel, handsome, witty, brave, good-humoured, but he is rich, rich, rich, rich, and rich— that one word contradicts everything you can say against him.”

-Henry Fielding

India is the world's most corrupt country. Black income is generated in India through various channels. Politicians and corrupt civil servants have deposited in foreign banks via illegal personal accounts. Black money stashed away in various tax havens such as Cayman Islands and Virgin Islands as also low or no tax countries such as Mauritius and Singapore. Cobra -Post sting operation brought into public the money laundering activities of HDFC bank, Axis bank and ICICI bank by last year.

Definition of **Informal Economy**

Informal economy is mainly supported by the black money generation. It has been generated via two major channels in India. **First**. Illegal means :**criminal activities**: which include kidnapping, smuggling, poaching, drug trade, illegal mining, income generated via terrorist activities, cheating and scams or maintaining disproportionate assets. **Corruption**: bribes and **theft** by public officers. **Second**: Hiding Income: Income not reported to authorities to evade tax. This mainly include real estate, finance, bullion and jewelry, equity trading.

Informal Economy and Black Income

Black Income is a term used in common parlance to refer to money that is not fully legitimate in the hands of the owner. This could be for two possible reasons.

- The income has been generated by illegitimate activities not permissible under the law, like crime, drug trade, terrorism and corruption all of which are punishable under the legal framework of the state.
- The second and perhaps more likely reason is that the wealth may have been generated and accumulated by failing to pay due to the public exchequer in one form or the another.

A comparison of the two ways in which black income is generated and is fundamental to understanding the problem and devising appropriate policy mix with which it can be prevented by the public authorities.

Black Money In India

An estimate by Suraj B. Gupta had put the size of black money at over 50 per cent of GDP (at factor cost) in 1987-88. It is also stated that annual rate of growth of black economy is higher than the annual growth rate of GDP. Now that black money constitute around 40% of the GDP.

According to Global Financial Integrity Study of 2009, \$ 1.4 trillion belongs to Indians were parked in safe havens abroad. \$ 1.4 trillion is equivalent to Rs. 70 lakh crore, more than India's national income of around Rs. 50 lakh crore.

A statement from the Swiss Central Bank declared that Indians have \$2.5 billion deposits in various Swiss Banks. It is suspected that the deposits of Indians in tax havens are mostly being withdrawn and shifted to a third country; making it difficult for the government to gather any further details once the accounts are closed.

Black money in Swiss banks¹- shows details of bank deposits in the territory of Switzerland by nationals of following countries:

COUNTRY	Estimate of Black Income
India	\$1,456 billion
Russia	\$ 470 billion
UK	\$390 billion
Ukraine	\$100 billion
China	\$ 96 billion

¹*Swiss Banking Association report, 2006*

India has more money in **Swiss bank** than all the other countries combined. Second best Russia has 4 times lesser deposit. US is not even there in the counting in top five. **609 people in India having legal property more than Rs- 100 crores (Rs- 10 Million). Indian President one day living cost is Rs-8 crore, living in a place where 350 flats. One day Indian Parliament running cost is around 9 crore Rupees. Britishers looted 350 Lakh Crore in 250 years whereas Indian himself looted 330 crore. 70 lakh crore only deposited in Swiss bank. 84000 corrupt people in India. India has around 450 Billion dollar of coal deposit & 170 billion of iron ore deposit, looted by state politicians .According to Indian Government around 1 Lakh place in India where people doing illegal mining.**

Indians' money in Swiss banks may have risen for the first time in five years, but they account for a meagre 0.14 per cent of total foreign wealth deposited there — putting India at 55th place globally for such funds. The total overseas funds in Switzerland's banking system stood at 1.53

trillion Swiss francs (about Rs. 90 trillion) at the end of 2011, which included 2.18 billion Swiss francs (Rs. 12,700 crore) belonging to Indian individuals and entities. While India accounted for only 0.14 per cent of total foreign money in Swiss banks, the U.K. accounted for the largest share of little over 20 per cent, followed closely by the U.S. with about 18 per cent.

As per the latest data disclosed by Swiss National Bank (SNB), Switzerland's central bank, India is now ranked 55th in terms of funds belonging to overseas clients in Swiss banks. Among the top-ranked jurisdictions, the U.K. and the U.S. were followed by West Indies, Jersey, Germany, Bahamas, Guernsey, Luxembourg, Panama and France, Hong Kong, Cayman Islands, Japan, Singapore, Australia, Italy, Netherlands, Russia, Saudi Arabia and United Arab of Emirates. The SNB data² shows that the quantum of money held by Indians in the Swiss banking system rose for the first time in five years during 2011.

INFORMAL ECONOMY AND TRADE RELATED MONEY LAUNDERING.

Trade-Related Money Laundering

Trade-related money laundering is an alternative remittance system that allows illegal organizations the opportunity to earn, move and store proceeds disguised as legitimate trade. Global trade is frequently

²Wikileaks Report

used by criminal organizations to move value around the world through the complex and sometimes confusing documentation that is frequently associated with legitimate trade transaction. Underground banking, unlicensed money service businesses, hawalas, etc., have all utilized trade to move value as settlement of a debt arising from remittances overseas. These organizations can accomplish settlement by purchasing commodities in one country and then transferring them to another country where the commodity is sold and the proceeds remitted to the intended recipient. Unlike tax avoidance and capital flight, which usually involve the transfer of legitimately earned funds across borders, capital movements relating to money laundering – or trade-based money laundering – involve the proceeds of crime, which are more difficult to track. Trade-based money laundering has received considerably less attention in academic circles than the other means of transferring value.

Channels of TRADE RELATED MONEY LAUNDERING

- **FII's**

Most foreign institutional investors are routing their investments into Indian stock markets through Mauritius. Many of them have formed shell companies³ that lack commercial substance, have no other commercial transactions and have been set up with the sole intention of making use of the double taxation avoidance agreement (DTAA) that Indian government has signed with Mauritius. Under this agreement investors pay capital gains tax in the country of domicile. Since Mauritius does not charge any capital gain tax on investments, these investors get off by evading Capital Gains Tax (CGT) altogether.

ROUND TRIPPING

Round tripping⁴ refers to routing of investments by a resident of one country back to his own country.

³ Shell companies: These are fake companies that exist for no other reason than to launder money. They take in dirty money as "payment" for supposed goods or services but actually provide no goods or services; they simply create the appearance of legitimate transactions through fake invoices and balance sheets.

⁴GAAR on Backburner for One Year, Chronicle

This is how it works: You get money out of India and transmit it to a tax haven with whom India has bilateral tax avoidance treaty. In the tax haven, this money is treated as capital of a registered entity. You now invest this money back in an Indian company as foreign direct investment FDI by using stakes or invest it in Indian equity markets. The entire purpose of this exercise is to window dress⁵ your original money which you had taken out from India as foreign capital. In the entire process, you end up paying zero or negligible taxes.

In India, you can claim tax exemption citing the double taxation avoidance agreement arguing that you have paid taxes in the source country. In the source country, taxes are negligible since it is a haven.

Capital market watchdog SEBI is looking into the possible use of PCCs from places such as Mauritius, Cayman Islands and Seychelles for use of round-tripping of Indians' money back into the capital market here in the form of overseas funds. In 2010, SEBI had barred Protected cell Companies (PCCs) to invest in Indian markets through Foreign Institutional Investor (FII) route after it came across instances where certain Indians had used these entities to route their money back into markets as FII funds. However, the market regulator now fears that funds structured as PCCs, which are legal entities in places like Mauritius, might be looking at a re-entry into Indian markets through routes like Foreign Venture Capital Funds and other avenues for the purpose of round-tripping of funds, a senior official said. PCCs are specially designed entities that might comprise of various cells, having funds of various investors, in such a manner that there is legal segregation and protection of assets and liabilities for each cell. Also, the insolvency of one cell does not affect the business of the entire PCC or that of the other cells. Besides getting tax-related benefits for being considered as a single entity despite having various cells, foreign banks in the past have been found to be hard-selling these schemes to their wealthy clients for the protection of identity as well, the official said. With an aim to safeguard the markets from any attempts of round-tripping of funds in contravention to the regulatory framework, SEBI is keeping a close eye on the foreign funds seeking to invest in the country.

⁵Window dressing: *Window dressing* is an attention-getting maneuver that can venture into unethical or illegal territory.

GAAR:

GAAR or General Anti Avoidance Rule is aimed at preventing deals or incomes that are structured only to avoid paying taxes. In India ,the courts have ruled that saving of taxes through permissible instruments of tax planning is legitimate. But tax avoidance is illegal.

Why FII's fear GAAR?

Foreign institutional investors have valid reason for being concerned about the imposition of GAAR. These rules will give the Income Tax authorities the power to look in to companies that lack substance and those that are set up mainly for tax avoidance. Structures used for mainly for round tripping would also have come under the tax –men's lens once GAAR was implemented.

Global practice on anti-avoidance rules:

Most countries have codified the substance over form “ doctrine in the form of GAAR” .Internationally several countries have introduced, and are administering statutory general anti avoidance provisions. The Indian Government is of the view that aggressive tax planning with the use of sophisticated structures ,there is a need to statutory provisions so as to codify an anti –voidance doctrine.

- **Insider trading**

Insider trading occurs when someone makes an investment decision based on information that is not available to the general public. In some cases, the information allows them to profit, in others, avoid a loss. Insider trading" actually includes both legal and illegal conduct. The legal version is when corporate insiders officers, directors, employees and large shareholders, buy and sell stock in their own companies. When corporate insiders trade in their own securities, they must report their trades to the SEC. Many investors and traders use this information to identify companies with investment potential, the theory being, if the insiders are buying the stock, they must know more about their company than everyone else, so it is a good idea to buy the stock. Insider trading is considered as a malpractice. The Securities and Exchange Board of India (SEBI) has fined certain corporatelike Reliance Industries group entity Reliance Petroinvestments (RPIL) for violating insider trading norms recently.

- **Money Laundering & IT in India**

Even today after the big burst of the Dotcom bubble almost every investor dreams of owning stocks of technology companies looking at their high growth potential and fantastic returns they provide. Since,

many of the infotech stocks are out of reach of the small investor considering their phenomenal prices; they rush for the smaller and the relatively cheap infotech stocks. But every company is not TCS or Infosys. Some of them are the shell companies which have the only business of laundering the money.

Many techies have started investing in the shares and they look for the attractive growth prospects. How do such companies operate and show decent earnings is the main question? There seems to be a kind of nexus between the export earnings of some technology companies and money laundering transactions. Many of these so-called software companies were known to be using the *Hawala*⁶ route in order to show income from software exports. Getting the knowledge about these transactions was not a big deal. It is provided to these companies by the CA's/Lawyers and other professionals who know the transactional loopholes. A Hawala transaction simply means that you pay rupees over here in India and in return get dollars abroad. For instance, if you want to do a Hawala transaction from Mumbai to USA, then by paying Rs 1 lac in Mumbai, you can transfer \$2500 in USA.

- **Banks and money laundering.**

There are many ways in which banks transform the black money into white were both imaginative in their range and brazen in their approach. This brought to the fore a modusoperandi that is tailored to rake in vast amounts of black money in the form of illegal deposits, insurance and investment products, sold by these banks. All these creative means make the dirty money squeaky clean without the regulatory authorities ever getting a whiff of what they are doing. Here is a gist of what the various bankers suggested to help the politician launder his illegitimate money.

1. Accept huge amounts of cash and invest it in insurance products and gold. Open an account to route the cash into various investment schemes of the bank.
2. Do it even without the mandatory PAN card or adhering to the KYC norms laid down by RBI.
3. Split the money into tranches to get it into the banking system without being detected.
4. Use "benami" accounts to facilitate the conversion of black money.
5. Use accounts of other customers to channelize the black money into the system for a fee.
6. Get demand drafts made for the client either from their own banks or from other banks to facilitate investment without it showing up in the client's account.

⁶Hawala: Hawala is an alternative or parallel remittance system and money transfer takes place without money movement.

7. Keep the identity of the investor/depositor secret.
8. Open multiple accounts and close them at will to facilitate the investment of black money.
9. Invest black money in multiple instruments in the names of different individuals, not necessarily drawn from among the family.
10. Allot lockers for the safekeeping of the illegitimate cash, including special large size lockers to accommodate crores of hard cash.
11. Personally come to the residence of the client to take the black money deal forward and collect the cash, even bring along counting machine.
12. Use provisions like Form 60 to deposit the illegitimate cash into the account to route it into investment.
13. Help the client to transfer black money abroad through Non-Resident External (NRE)/ Non-Resident Ordinary (NRO) account; transfer the money telegraphically or through means other than regular banking procedures.

CORPORATE AND MONEY LAUNDERING IN INDIA

Corporate structures are misused to evade taxes and thereby generate black money.

Operation Red Spider

A Cobrapost pan-India undercover investigation spanning several months, unearths a vast, nation-wide money laundering racket being run by HDFC Bank, ICICI Bank and Axis Bank. The brazen criminal activity by these banks is channelizing vast amounts of black money into the regular banking system as laundered white money. Investigation, conducted across dozens and dozens of branches of these banks and their insurance affiliates, across all five zones of the country, revealed these shocking facts:

That these money laundering practices are part of a standard set of procedures within these banks;

- ▶ These money laundering services are being openly offered to even walk-in customers who wish to launder their illicit money.
- ▶ A variety of options for laundering ill-gotten cash are being offered brazenly.
- ▶ These money laundering services are being offered practically as a standard product across the country.

This huge money-laundering racket being run by these banks has been captured by Cobrapost, on videotape, running into hundreds of hours. The evidence is graphic, crystal-clear and clinching. The investigation finds the banks and their managements systematically and deliberately violating

several provisions of the Income Tax Act, Know Your Customer (KYC) norms, RBI regulations, Foreign Exchange Management Act (FEMA), the Banking Act and Prevention of Money Laundering Act (PMLA) with utter disregard to consequences, driven by their desire to boost cheap deposits and thereby increasing their profits. It puts a big question mark on the legitimacy of these banks' deposits and therefore their profits. It also raises grave questions of the legitimacy and origins of funds being raised in their insurance and investment arms. It is also clear from our investigations that these banks have been indulging in these criminal practices for several years and have well-oiled processes for the same.

Harshad Mehta (1992) Securities scam

Mehta gradually rose to become a stock broker on the Bombay Stock Exchange and had an expensive lifestyle. Through the second half of 1991, Mehta had earned the sobriquet of the 'Big Bull', because he was said to have started the bull run. On April 23, 1992, journalist Sucheta Dalal exposed Mehta's illegal methods in a column in The Times of India. Mehta was dipping illegally into the banking system to finance his buying.

The game went on as long as the stock prices kept going up, and no one had a clue about Mehta's modus operandi. Once the scam was exposed, the banking system had been swindled of a whopping Rs 4,000 crore. The Chairman of the Vijaya Bank committed suicide by jumping from his office roof. He knew that he would be accused if people came to know about his involvement in issuing cheques to Mehta. Mehta made a brief comeback as a stock market guru in 1998, giving tips on his own website as well as a weekly newspaper column. This time around, he was working with owners of a few companies and recommended only the shares of those companies. This game, too, did not last long. By the time he died, Mehta had been convicted in only one of the many cases filed against him.

Hawala Diaries (1996)

The Hawala scandal involved payments allegedly received by politicians through hawala brokers, the Jain brothers. It was a Rs 70 crore bribery scandal that implicated some of the country's leading politicians. There were also alleged connections with payments being channelled to Hizbul Mujahideen militants in Kashmir.

The scandal surfaced following CBI raids on hawala operators in Delhi in 1991. The accused included LK Advani, VC Shukla, P Shiv Shankar, Sharad Yadav, Balram Jakhar and Madan Lal Khurana. Many were

acquitted in 1997 and 1998, partly because the hawala records (including diaries) were judged in court to be inadequate as the main evidence. The failure of this prosecution by the Central Bureau of Investigation has been widely criticised. But it was S.K. Jain's diaries that had heads rolling.

KETAN PAREKH & THE STOCK MARKET CASE (2001)

Parekh's party ended rather abruptly a day after the Union Budget was presented in February 2001. A bear cartel started disrupting Parekh's party by hammering prices of the K-10 stocks,

precipitating a payment crisis in Kolkata. He is a chartered accountant by training, Ketan Parekh came from a family of brokers. Between 1999 and 2001, as the technology bubble was engulfing the rest of the world, the stock market in India sprang to life too. Be it investment firms, mostly controlled by promoters of listed companies, overseas corporate bodies or cooperative banks, all were ready to hand the money to Parekh, which he used to rig up stock prices by making his interest apparent. In no time, scrips like Visual soft rose from Rs 625 to Rs 8,448 per share and Sonata Software from Rs 90 to Rs 2,150. But the vicious cycle of fraud did not end with price rigging. The inflated stocks had to be dumped onto someone in the end, for which Parekh used financial institutions like the UTI.

As SEBI investigated, it was evident that bank and promoter funds were used to rig the markets. In March 2011, the mayhem wiped off over Rs 1,15,000 crore from the markets. Parekh was arrested in March that year and was in custody for 53 days. Currently he has been debarred from trading in the Indian stock exchanges till 2017. In the aftermath of the scam, many gaping loopholes in the market were plugged. The trading cycle was reduced from one week to one day. Badla was banned and operators could not carry forward trade in its primitive form. Forward trading was formally introduced in the form of exchange-traded derivatives to ensure a well-regulated futures market. Broker control over stock exchanges was demolished.

It's perhaps thanks to the Pentafour Bull that India's stock markets are today considered safe. And to his credit, Parekh forced lethargic policy-makers to institute reforms in the financial system.

IPO demat scam (2005)

An IPO is the first sale of an entity's common shares to public investors. When an entity wants to enter the market, it makes its share available to common investors in form of an auction sale. Each application

for an IPO has to be within a cut-off figure, which is eligible for allotment in the retail investors' category. But in this case, financiers and market players illegally cornered these retail investors' shares.

The IPO scam came to light in 2005 when the private 'Yes Bank' launched its initial public offering. Roopalben Panchal, a resident of Ahmedabad, had allegedly opened several fake demat accounts and subsequently raised finances on the shares allotted to her through Bharat Overseas Bank branches. The SEBI started a broad investigation into IPO allotments for YES bank in 2005. Apart from the YES Bank fraud, SEBI reportedly has definite data about two IPOs where retail allotments were rigged, but market observers believe the scam is far bigger. The Income-Tax Department in Ahmedabad has found that two major accused, Panchal and Sugandh Investments, have together made Rs 60.62 crore in 18 months.

Satyam Scam (2009)

In January 2009, Raju indicated that Satyam's accounts had been falsified over a number of years. He admitted to an accounting dupery to the tune of Rs 7,000 crore rupees and resigned from the Satyam board on January 7, 2009. Raju and his brother, B Rama Raju, were then arrested by the Andhra Pradesh police. Raju was convicted of cheating six million shareholders and is being held in Hyderabad's Chanchalguda jail on charges including embezzlement, insider trading, breach of trust, conspiracy, cheating, and falsification of records.

Black Money and Hassan Ali Khan (2009)

Hassan Ali is allegedly worth \$9 billion or more, according to law authorities. The Government of India has also confirmed the existence of this account in UBS, and ordered him to pay Rs 50,000 crore in taxes on that wealth. However, according to Khan, he is a scrap dealer with an annual income of Rs 30 lakh. Some sources claim that he might be the fourth richest person in India and amongst the world's dollar billionaires. The Enforcement Directorate, Income Tax department along with the Economic Offences Wing (EOW) of Maharashtra are probing the illegal investments and charges of money laundering against Khan. The Supreme Court of India questioned the Central Government's inertia on this issue. Despite this, the Central Government doesn't intend to prosecute Khan under India's money laundering law simply because it hadn't gone into effect at the time the alleged crimes were committed.

POLICY IMPLICATIONS

White paper on black money

The white paper on black money was tabled in Lok Sabha on May 21, 2012 by the Finance Minister, Pranab Mukherji. The paper suggests the policy options that could be pursued by the centre and the states to tackle the menace.

It has identified certain sectors—real estate, finance, bullion, and jewellery, equity trading, mining – as being prone to black money generation. The 97 page document does not reveal names of Indians who have stashed black money abroad. It recommends certain controversial policy options such as suggesting that states governments levy agricultural income tax and asking SEBI to tighten reporting norms on Participatory norms.

The Finance Minister while responding to an adjournment motion on the situation *Arising out of Money Deposited Illegally in Foreign banks and Action being Taken against the Guilty persons* in the Lok Sabha on 14 December 2011 gave an assurance that a paper on black money would be prepared. Hence the document is presented to Parliament as a result.

Reforms in sectors Vulnerable to Generation of Black Money

A large proportion of black money is generated from certain vulnerable sectors of economy suggesting that effective reforms in those sectors can be a major strategy for curbing generation of black money.

Financial Sector

The financial sector is the most important sector in the economy when it comes to transfer of funds generated through whatever means into further productive activities. Therefore it is one sector that cannot possibly remain untouched of black money. Fine tuning of financial regulation

therefore remains one of the key areas in creating deterrence against generation of black money in the process being laundered. Significant progress made in the efficacy of the oversight mechanism for financial markets needs to be pursued further.

For this purpose it is essential that the relevant authorities are able to get trained manpower with proper domain knowledge of financial investigation and oversight. One of the solutions could be to place efficient officials with requisite domain knowledge and skills from the financial investigative agencies in the operations/vigilance machinery of banks and financial institutions to keep proper vigil and ensure that rules and regulations are followed in these institutions.

Real estate

The real estate sector in India constitutes about 11 per cent of the GDP. Investment in property is a common means of parking unaccounted money and a large number of transactions in real estate are not reported or are under-reported. This is mainly on account of very high levels of property transaction taxes, commonly in the form of stamp duty.

High transaction taxes in property are one of the biggest impediments to the development of an efficient property market. With tax rates of over 5 per cent being imposed as stamp duty of property, which otherwise also involves high transactions costs in terms of search, advertising, commissions, registration, and contingent costs related to title disputes and litigation, property market remains one of the inefficient asset markets in India.

To reduce the element of black money in transactions relating to immovable property and facilitate focused action based on actionable intelligence by monitoring agencies, simple reporting systems can be involved that will facilitate the development of a nationwide database. One of the measures for deterring use of the real estate sector for generation and investment of black money could be the provision of deducting tax at source on payments made on real estate transactions and mandating it as a pre-condition for registering systems in this sector.

Bullion and Jewellery sector

Bullion and jewellery is an important sector for both generation and consumption of black money and is also targeted by black money holders looking towards protecting the value of their black money from inflationary depreciation. Moreover, a fairly large number of transactions in this sector remains totally unreported and therefore facilitate investment and consumption of black money. There is also urgent need to improve the reporting and monitoring systems in this sector.

Cash Economy

Cash has always been a facilitator of black money since transactions made in cash do not leave audit trail. So far, efforts to regulate and control cash transactions have been constrained. So far efforts to regulate and control cash transactions have been constrained due to two reasons. The first is that the poor have to deal in cash, particularly in the rural sector, and accordingly payments on account of labour wages or those made to rural artisans and institutions need to be made in cash. Second, the costs of transaction imposed by any regulations are likely to spread across the economy and affect both consumers and producers, thereby leading to resistance and lack of support for such a move.

Strategies for curbing generation of black money

In most of the cases people who are indulged in black money generation are not indulging in activities that are criminal in themselves. In such cases treat a person generating black money as a rational economic agent who can be made to comply with the law by creating appropriate incentives and disincentives in favour of reporting and tax compliance.

Reducing Disincentives against Voluntary Compliance

There can be several factors that incentivize a person against reporting his income or wealth. Primarily, they consist of the cost that person incurs in complying with the law and its reporting regulations. The costs consist of two major components, the tax that needs to be paid as part of the compliance and the costs that need to be incurred in addition to the taxes for complying with the regulatory obligations. Both of them are important disincentives and reducing them can improve disclosure and lessen the generation of black money.

Rationalization of Tax Rates

The higher the tax, higher is the disincentives against tax compliance and greater the propensity to generate black money. Thus reducing tax rates, particularly the maximum marginal rates of progressive tax, can increase tax revenue in two ways, first by increasing tax base and second by increasing compliance with the tax rules and thus can be one of the major policy tools for curbing the generation of black money.

Reducing Transaction costs of Compliance and Administration

The high transaction cost associated with compliance with the law and regulation is the other major disincentive that hinders compliance and pushes people towards generation of black money. It includes the opportunity cost of time and resources to the tax payer and tax administration.

It may be possible in India too to signify cut down the costs of compliance borne by the citizens, by raising the cost of administration to some extent. Simply put ,investments in improving administrative facilitation of compliance with tax and other regulatory measures may leads to positive gains to society

The Prevention of Money Laundering Act, 2002 (PMLA) was enacted in 2003 and brought into force on 1st July 2005 to prevent money laundering and to provide for attachment, seizure and confiscation of property obtained or derived, directly or indirectly, from or involved in money laundering and for matters connected therewith or incidental thereto.

Prevention of Money Laundering (Amendment) Bill, 2011 was introduced in Parliament and subsequently referred by the Speaker, Lok Sabha to the Standing Committee on Finance of Parliament on 5 January, 2012 .

DTAA:

These are bilateral treaties signed between governments to prevent companies from paying taxes both in their country of origin as well as in the country where they are doing business. Under this agreement investors pay any capital gain tax in the country of domicile, since Mauritius does not charge any capital gain tax on investment they get off by evading tax together. India has made an agreement of double taxation with Mauritius.

GAAR:

The GAAR Rule was proposed in mid March as part of the Budget for fiscal 2013. GAAR aims to target tax evaders partly by stopping Indian companies & investors from routing investments via Mauritius or other tax haven by avoiding tax. F.M rolled out GAAR till 2013 to provide more time to tax payers and tax officers to address all related issues. Committee under chairmanship of director general of income tax and formulating guidelines for implementing GAAR.

ParthasarathyShome Final Report

The final report submitted on 1st Oct,2012.India would finalise guidelines on its commercial anti avoidance law with 20 days after considering recommendations by a government panel.

Shome Panel Recommendations on GAAR

- 1.GAAR to include all nonresident tax payers.
- 2.Changes in the Income Tax Act & Rules.
- 3.Implementation of GAAR may be deferred by 3 years on administrative grounds.
- 4.Abolish transfer gains arising from transfer of listed securities.
- 5.GAAR is to be applicable only in cases of abusive ,contrived and artificial arrangement.
- 6.Should not be involved in intra group transactions.
- 7.Tax audit report may be amended to include reporting of tax avoidance schemes above a specific threshold of tax benefit 3 crore and above.
- 8.GAAR provisions should not be involved to examine the genuineness of the residency of entities in Mauritius.

Conclusion

Thus the impact of informal economy and the effects of trade related money laundering can be summarized. Unaccounted income has been causing underestimation of GDP in India and a major part of income is diverted to this unaccounted sector via round tripping or money laundering activities , resulting in the expansion of parallel economy of the country. The direct effect of money laundering is the loss of revenue to the state exchequer by tax evasion. Further results in transfer of funds from India to tax havens in foreign countries . The generation of black incomes in the economy results in widening inequalities of income distribution and hence leaves a large amount of funds at their disposal. This money have found unscrupulous uses. Thus the existence of informal economy has totally destroyed the planning of the economy.All Planning and policies are meaning less unless we control illegitimate creation and use of money .

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