

Black Money and Demonetisation

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ABSTRACT: *This paper has focus on the black money and its effect of demonetisation and law related to black money. Discuss the Income Declaration Scheme 2016 (IDS'2016) and define its deferent section including the Tax and surcharge. Define Black Money Act'2015, its prosecution and eight steps of surgical strike against black money. Mainly focus on comparative analysis between the Income declaration Scheme 2016 v. Black Money Act, provision U/s 271 (1) & 276 (C) and provision U/s 270A.Importance of prevention of Money Laundering Act 2002 and its feature with similar law in other countries.*

Keywords: *Black Money, Demonetisation, IDS'2016, Money Laundering, Surgical Strike.*

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I. INTRODUCTION

Black Money: Black Money is a term used to refer to money that is not fully legitimate in the hands of the owner. A definition of black money was adopted in the White paper issued on Black Money by Government of India in May 2012. “Black money is defined as assets or resources that have been reported to the public authorities at the time of their generation not disclosed at any point of time during their possession.” Black money could arise broadly due to two possible reasons. The first is that the money may have been generated through illegitimate activities not permissible under the law, like crime, drug trade, terrorism and corruption, all of which are punishable under the legal frame work of the state. Some of these offences are included in Prevention of Money Laundering Act 2002. The second and perhaps more likely reason is that the wealth may have been generated and accumulated by failing to pay the dues to the public exchequer in one form or other has failed to report the income generated or comply with the tax requirements or pay the dues thereby converting such income into black money.¹

Black Money and Demonetisation: The Government of India announced that Rs. 500 & Rs. 1000 denominated currency notes will cease to be legal tender. The move was targeted toward tackling black money, corruption and terrorism. To start off, black money is a wider societal ill and demonetisation is but one step in the war against black money. Black money and black economy are also two different constructs. The term shadow economy and underground economy are also used as synonyms for black economy. The issue of black money has been well explored. The National Institute of Public Finance and Policy has been active in research about black money in their survey. Black money is nothing but money generated in legitimate transaction which is hidden from government so as to avoid paying the transaction cost (usually tax) in the legitimate economy, this is usually done by using physical cash. Black money is also used in legitimate investment, foreign channels play critical role, quite substantial investment in P notes is actually round tripped black money. The key aspect of these instrument is create anonymity by begin away from arms of the laws of the country from where income can be fed into the legitimate hands. In such cases, the source of income is illegal, thus many businesses in tax havens such as Mauritius, Cayman Islands etc. exist to convert illegal money into legal money and many of these investments come under the purview of money laundering. The distillation of various approaches for tackling of black money such as , establish identity of person, enable low the cost direct bank transfer, reform tax system (GST), auto processing returns for tax refund, create attribute chain for funds entering and exiting the country, control of holding of cash and physical money. As per RBI estimates, 15 billion notes of 500 and 6 billion notes of 1000 denomination exist. In addition, RBI estimates that fake 0.2 million notes of Rs. 500 and 0.15 million notes of Rs. 1000 were discovered. Those who can disclose deposits equal to the amount they hold in cash will have no problem. Part of the actual money in circulation is never recovered, depending on various conditions at least 20% of this paper money will never reach banks. This stock of money is lost; many believe this to be deflationary. This money did contribute to the economy but to smaller extent. Black money is not a pool but a chain, break the chain or make the chain costly and you inconvenience the poor who did not have

¹ “Black money”, retrieved on 29/05/2017, http://arthapedia.in/index.php?title=Black_Money, pp 1-3

access to bank systems, but with Jan Dhan accounts, poor have ready access to banking channels. So if you are law abiding citizen then you can sail through mostly unscathed no matter how poor you are. Real estate, Gold etc., driven consumption is out of purview of the legitimate formal economy. The effect of demonetisation on such consumption will be positive. The issue in present case is the quantum of readjustment, if RBI balance sheet shrinks by 30% on fine day, there will be panic, but this effect can also be muted by writing down in phased manner while keeping the liability alive on paper, if this was possible you could have seen demonetisation every 5 years. The actual terror attack is only the “last mile” effect, the ultimate attackers are usually pawns without any knowledge of systems, it will serve to shock this chain. Demonetisation eliminate black money is just one move of one piece in the chess board of black money to check mate the black money king, you have to win the board there are various steps required.²

White money is being constantly converted into Black money and vice versa. Much of conspicuous consumption is paid for in unaccounted money which, in the hand of the recipients become perfectly legal income. “Benami” deals on the stock exchanges and commodity markets make it difficult to trace the transactions to the ultimate buyer or seller. Even if the existing stock of illegal currency is wiped out by demonetisation, it will be soon replaced as long as such points of contact exist between legitimate and illegitimate deals. Ultimately the problem of undisclosed income and wealth has to be tackled at the source. The major requirement is for the Government to reduce the opportunity for such transaction by generally reducing the gap between the market valuation of goods and the officially fixed prices. A check of inflation would be more effective than anything else in eliminating opportunities for speculative profit and black market deals.³

Law on Black Money: Government to enact a comprehensive new law on black money to specifically deal with black money stashed away abroad in the Black Money (Undisclosed Foreign Income and Assets) Imposition of Tax Bill, 2015. Government has also introduced the Benami Transaction (Prohibition) Amendment Bill, 2015 to amend the Benami Transaction Act, 1988. Prevention of Corruption Act, 1988. Prevention of Money Laundering Act, 2002. Also proactively engages with foreign government with a view to facilitate and enhance the exchange of information under Double Taxation Avoidance Agreements (DATAAs), Tax Information Exchange Agreements (TIEAs), Information sharing arrangement with USA under its Foreign Account Tax Compliance Act (FATCA), as on 30.06.2016, India has tax treaties (bilateral or multilateral) with 139 countries/offshore jurisdiction.⁴

The Income Declaration Scheme 2016

Last year Indian Government introduced a scheme for voluntary declaration of undisclosed foreign income and assets for resident taxpayers under the Black Money Act. A similar scheme is proposed by the Finance Bill, 2016 referred as “Income Declaration Scheme 2016” (IDS 2016).⁵ A declaration in respect of any income chargeable to tax under the Income tax act for any assessment year prior to the assessment year beginning on the 1st day of April 2017, for which he has failed to furnish a return under section 139 of the Income tax act, which he has failed to disclose a return of income furnish by him under the Income tax Act before the date of commencement of this Scheme. No deduction in respect of any expenditure or allowance shall be allowed against the income in respect of which declaration under this section is made.

Charge of tax, surcharge and penalty: Notwithstanding anytime contained in the Income tax Act or in any Finance Act, the undisclosed declared under section 183 within the time specified therein shall be chargeable to tax at the rate of 30% of such undisclosed income and the amount tax chargeable under sub section (1) shall be increased by a surcharge for the purpose of the Union to be called the Krishi Kalyan Cess on tax calculated at the rate of 25% of such tax as to fulfil the commitment of the Government for the welfare of the farmers. In addition to tax and surcharge under section 184 be liable to penalty @25% of such tax.

Section defined under IDS 2016

1. Section 188, undisclosed income declared not to be included in total income.
2. Section 189, undisclosed income declared not to affect finality of completed assessments.

² “Black money and demonetisation”, retrieved on 06/04/17, <http://www.rahuldepdhar.com> , pp 1-22

³ “Demonetisation and Black money”, Economic and political weekly, vol.2 No. 19, <http://www.jstor.org/stable/4357924>, pp 868-A 869

⁴ “Black Money”, retrieved on 29/05/17, http://arthapedia.in/index.php?title=Black_Money, pp 1-3

⁵ “The Income Declaration Scheme 2016”, Lakshmi Pawan, Lakshmikumaran & Sridharan, Hyderabad, pp 1-5

3. Section 190, undisclosed income declared not to be treated as benami transaction in certain cases.
4. Section 191, tax in respect of voluntarily disclosed income not refundable.
5. Section 192, declaration not admissible in evidence against declarant.
6. Section 193, declaration by misrepresentation of facts to be void.
7. Section 194, exemption from wealth tax in respect of assets specified in declaration.
8. Section 195, applicability of certain provision of Income Tax Act and of chapter V of the Wealth tax Act.
9. Section 196, scheme not to apply to certain persons.
10. Section 197, removal of doubts.
11. Section 198, power to remove difficulties.
12. Section 199, power to make rules.⁶

Prosecution: Declaration of past undisclosed income in the current year amounts to false verification of return of income which shall attract prosecution under the IT Act. If a taxpayer attempts to declare past undisclosed income in the current year, he will have to explain the source of income and substantiate the manner of earning the said income. In case of disclosed under the IDS there is no need to explain the source of income, the CBDT (Central Board of Direct Taxes) added. The IDS-2016 provides a four month window for domestic black money holders to disclose their assets and come clean by paying 45% tax and penalty. The compliance window close on September 30 and tax is to be paid by November 30, 2016. The IT department is in receipt of large volume of information from various sources such as registrar of property, banks, financial institution, stock exchange, tax deductors etc. The department has launched a comprehensive data mining and compliance management programme which will generate a large volume of information about financial transaction undertaken by taxpayer and the relevant year in which the transaction was undertaken. In order to make IDS a success the CBDT has been trying to give the scheme wide publicity, it also launched a you tube advertisement and TV commercial explaining the benefit of the scheme.⁷

Black Money Act, 2015

It extends to whole of India & shall come into force on the 1st day of April 2016. The highlight of Black Money Act 2015 is as under:-

Basis of Charger: There shall be charged on every assesses a tax in respect of his total undisclosed foreign income & assets of the previous year @30%. Value of undisclosed assets, FMV of an asset. No deduction shall be allowed of any expenditure. Tax authority shall same as specified under Income tax Act'1961. The powers regarding discovery & production of evidence for the purpose of this act, the tax authority have same powers as are vested in a court under CCP (code of civil procedure).

For assessment: AO shall be perform duties of assessment, order must be issued before the expiry of two years from the end of financial year in which notice was issued. Tax authority may amend order to rectify the mistake apparent from record with in four year from the end of financial year in the order sought to amend was passed, direct assessment or recovery is not barred in this act. Appeals shall hear and determined in the appellate tribunal against such order within 60 days from the date of order passed.

Mode of recovery of tax dues: The AO or tax recovery officer may require any debtor of the assesses to pay such amount not exceeding the debt, if the assesses shall not pay the tax arrear with in prescribed time or extended time, then AO may pass a certificate to recovers the tax to tax recovery officer. If there is default in furnishing of return of income (Foreign undisclosed income) & non-payment of tax or determent of advance tax, interest shall be payable under section 234A/234B/234C of income tax act 1961. Penalty in relation to 3 times of the tax computed. Chapter V of this act contains of offence & prosecutions. Chapter VI of this Act contains tax compliance for undisclosed foreign income and assets. Chapter VII of this Act contains general provision.⁸

Eight steps of surgical strike against black money

Prime Minister pulled off a major coup today to check black money, he had laid its foundation over two years ago, he waited for the festival season to get over to take eight steps of surgical strike against black money.

⁶ "The income declaration scheme 2016, chapter ix of the Finance Act 2016", retrieved on 29/05/17, <http://www.incometaxindia.gov.in/pages/ids-2016.aspx>, pp 1-6

⁷ "Black money discloser in AY 17-18 to face prosecution", retrieved on 29/05/17, <http://www.indianexpress.com>india>, pp 1-3

⁸ "Black money Act 2015", retrieved on 29/05/17, <http://www.taxguru.in/income-tax/highlights-black-money-act-2015.html>. pp 1-2.

1. SC-monitored SIT on Black Money: Constituted a Supreme Court Monitored special investigation team (SIT) on black money.
2. Jan Dhan Yojana: This was followed by the launch of the PMJDY on August 28, 2014. Till date 25.45 crore accounts have been opened so far and Rs. 45, 302.48 crore has been deposited in these accounts. A total of 20.28 crore accounts have been opened in the public sector banks of the 11.39 crore accounts in the rural areas while 8.90 crore accpounts in the urban areas.
3. Renegotiation of Tax Treaties and Automatic Information Exchange Agreements with Tax Havens: The government renegotiated the DTAA with Mauritius to impose Capital Gains Tax if such Capital Assets is situated in India. The government also negotiated with Switzerland and other tax havens.
4. The Black Money (Undisclosed Foreign Income and Assets) and Imposition of Tax Act 2015 for Foreign Black Money: The scheme was launched to bring back black money stashed in foreign countries and tax havens, the Act also had various stringent provision for penalty and prosecution of foreign black money holders unearthed during future investigation by the tax department.
5. Income Disclosure Scheme 2016: The IDS which opened gave a chance to black money holder to come clean by declaring the assets by September 30 and paying tax and penalty of 45 percent on it. Income tax department identified 90 lakh high value transaction without PAN, the final disclosure of black money was to the tune of Rs. 65,250 crore.
6. Penalty on Real Estate Transaction undertaken in Cash exceeding Rs. 20,000: Imposed a penalty of 20% on all cash transactions exceeding Rs. 20, 000/- to purchase or sell a property (real estate). This was aimed at curbing the role of black money in real estate trasactions.
7. Tax collection at source on Cash Sales exceeding Rs. 2 lakh: Another important step to check high value cash transaction and create an audit trail was to impose Tax collection at source at a nominal rate of 1% on cash purchases exceeding Rs. 2 lakh.
8. Benami Transaction (Prohibition) Amendment Bill: The Parliament passed the Benami Transaction (Prohibition) Amendment Act, 2016 (BTP Amendment Act) in August. It came in to force from November 2016 notification issued by the Income Tax Department.⁹

The Income declaration Scheme 2016 v. Black Money Act, provision U/s 271 (1) & 276 (C) and provision U/s 270A

In this point discuss the possible benefits available to the taxpayer under the IDS 2016 comparing the provision of Black Money Act, existing penal provision under section 271 (1) & u/s 276 (C) and proposed penal provision under section 270A.

Comparison 1: IDS 2016 v. Declaration under Black Money Act

In the Black Money Act the taxpayer was required to pay up to 60% as both tax and penalty under that scheme. Now a new IDS 2016 scheme the taxpayer was required to pay up to 45% as to pay tax, surcharge and penalty of such undisclosed income declared.

As the net liability to be discharged under the IDS 2016 is lower than the declaration made under Black Money Act, IDS 2016 it obviously appears to be more beneficial.

Comparison 2: IDS 2016 v. Provision under section 271(1) & 276C

Any wilful attempt to evade tax under the current provision of the Act attract penalty under section 271 and prosecution under section 276, it would be ranging from 100% to 300% of the amount of tax sought to be evaded. However, under the IDS 2016 the penalty will be just 25% of the tax evaded (i.e. 25% of 30%) and the declarant will be deemed to be immune from all prosecution proceeding under the Income Tax Act and Wealth Tax Act. As the total liability to be discharged under IDS 2016 is thus lower that total liability to be discharged considering the provision of section 271 & 276.

Comparison 3: IDS 2016 v. Provision under section 270A

The proposed section 270A seeks to provide that the tax officer may levy penalty if a person has under reported his income cases where income assessed is greater than the income determined under section 143(1) or where income assessed is greater than the maximum amount not chargeable to tax, if no return has been furnished or where income assessed is greater than the income assessed or reassessed immediately before such re-assessment etc.

Penalty in any of the above referred cases shall be equal to 50% of the amount of tax payable on under reported income. However in case of any misreporting of income the penalty will increase from 50% to 200% of the amount of tax payable on under reported income. Under the IDS 2016 the penalty will be just 25% of the tax evaded (i.e. 25% of 30%) and the declarant will be deemed to be immune from all prosecution proceeding under

⁹ "Surgical Strike against Black money", retrieved on 29/05/17, <http://www.indiatoday.intoday.in>india>, pp. 1-2

the Income Tax Act and Wealth Tax Act. The total liability under IDS 2016 is lower than total liability to be discharged under the proposed Section 270A. The above comparison described with given example.

Particular	Section 271 & 276	Section 270A	IDS 2016
Basic Tax Rate (assuming a company)	30%	30%	30%
Surcharge	7%	7%	25% to 30%
Education Cess	3%	3%	-
Penalty	100% to 300%	50% / 200%	25% to 30%
Prosecution	Yes, but compoundable	No / Yes	Immunity granted

IDS 2016 is definitely a beneficial scheme for the eligible tax payer to declare the income which was not offered to tax earlier. However one should note that the immunity from prosecution granted is only under Income Tax Act and Wealth Tax Act, but not under Foreign Exchange Management Act.¹⁰

Prevention of Money Laundering Act 2002

Prevention of Money Laundering Act 2002 is an Act of the parliament of India enacted to prevent money laundering and to provide for confiscation of property derived from money laundering. PMLA and the rules notified there under came into force with effect from July 2005. The act and rules notified there under impose obligation on banking companies, financial institutions and intermediaries to verify identity of client, maintain records and furnish information in prescribed form to Financial Intelligence Unit-India. The PMLA seeks to combat money laundering in India and has three main objectives:

1. To prevent and control money laundering.
2. To confiscate and seize the property obtained from the laundered money.
3. To deal with any other issue connected with money laundering in India.

Salient features

Punishment for Money laundering: The act prescribed that any person found guilty of money laundering shall be punishable with rigorous imprisonment from three years to seven years and where the proceeds of crime involved related to any offence under the schedule (offences under the Narcotic Drugs and Psychotropic Substance Act 1985) the maximum punishment may extend to 10 years instead of 7 years.

Power of Attachment of tainted property: Appropriate authorities appointed by the Govt of India can provisionally attach property believed to be proceeds of crime for 180 days, such an order is required to be confirmed by an independent adjudicating authority.

Adjudicating Authority: The Adjudicating Authority is the Authority appointed by the central government through notification to exercise jurisdiction power and authority conferred under PMLA, it decides whether any of the property attached or seized is involved in money laundering.

Presumption in inter connected transaction: Where money laundering involves two or more inter connected transaction and one or more such transaction is or are proved to be involved in money laundering then for the purposes of adjudication or confiscation it shall be presumed that the remaining transaction from part of such inter connected transaction.

Burden of proof: A person who is accused of having committed the offence of money laundering has to prove that alleged proceeds of crime are in fact lawful property.

Appellant Tribunal: An Appellant Tribunal is the body appointed by Govt of India, it is given the power to hear appeals against the order of the Adjudicating Authority and any other authority under the Act. Order of the Tribunal can be appealed in appropriate High Court and finally to the Supreme Court.

Special Court: Section 43 of Prevention of Money Laundering Act 2002 says that the Central Government in consultation with the Chief Justice of the High Court shall for trial of offence punishable under section 4 by notification, designate one or more Courts of Session as Special Courts for such area or areas or for such case or class or group of cases as may be specified in the notification.

FIU-IND: Financial Intelligence Unit-India (FIU-IND) was set by the Government of India on November 2004 as the Central National Agency responsible for receiving, processing, analyzing and disseminating information relating to suspect financial transaction. FIU-IND is also responsible for coordinating and strengthening efforts of national and international intelligence. FIU-IND is an independent body reporting directly to the Economic Intelligence Council (EIC) headed by the Finance Minister.

¹⁰ "The Income Declaration Scheme 2016- An analysis", Lakshmi Pavan, Principal associate, Direct tax practice, Lakshmikumaran & Sridharan, Hyderabad, pp. 1-5.

Similar laws in other countries

Money Laundering Control Act of 1986 is an act of the United States Congress that made money laundering a Federal crime, it criminalised money laundering for the first time in the United States. Established money laundering as a federal crime. Prohibited structuring transaction to evade CTR filling. Introduced civil and criminal forfeiture for BSA violations. Directed banks to establish and maintain procedures to ensure and monitor compliance with the reporting and record keeping requirement of the BSA.¹¹

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¹¹ “The prevention of Money Laundering Act 2002”, retrieved on 05/06/2017, http://www.fiuindia.gov.in/downloads/PMLA_2002.pdf, pp. 1-4.