IJCRT.ORG ISSN : 2320-2882

INTERNATIONAL JOURNAL OF CREATIVE RESEARCH THOUGHTS (IJCRT)

An International Open Access, Peer-reviewed, Refereed Journal

TAX EVASION AND TAX AVOIDANCE - IMPACT OF INDIAN ECONOMY

Ishwarya.S

BBA.LLB (Hons)

Sastra Deemed To Be University

ABSTRACT

Tax evasion and tax avoidance are two practices that have significant effects on the Indian economy. Tax evasion includes engaging in illegal activities to avoid paying taxes in full. Both tax avoidance and tax evasion cause a loss of government revenue, which may restrict governmental spending on infrastructure, social welfare, and development programmers. Tax avoidance refers to the legal exploitation of tax law loopholes to minimize tax liability. Income disparity is also worsened by tax avoidance and evasion, which also damages public trust in the tax system. In the past, the tax evasion and tax avoidance of a large informal sector, poor tax administration, and complicated tax laws have allowed tax evaders to thrive, resulting in significant revenue losses that have made it difficult for the government to fund public services.

The Indian government has implemented a number of measures that target tax avoidance and evasion in the current situation. These include improving tax legislation, enhancing tax administration, and utilizing technology to increase compliance and transparency. Tax evasion is being battled and a tax system that is more equitable is being promoted through initiatives such as demonetization, the implementation of the Goods and Services Tax (GST), and the creation of the Direct Tax Code. This paper explores multi dimensions of tax avoidance and tax evasion in the view of current government laws, policies and preventive measures, how it has affected the Indian economy and the judicial interpretation of tax evasion and avoidance.

KEY WORDS: Tax payer, Tax evasion, Tax avoidance, Impact of economy, penalties.

INTRODUCTION

Tax evasion is where individuals deliberately fail to pay the tax liability. For example, if the taxpayer fails to pay tax that is imposed on him or if he pays the tax less than the tax that is imposed on him it becomes an illegal act and it's a tax fraud it is called tax evasion. Whereas tax avoidance means the taxpayer through the advantage of the legislature and through the loopholes in it he reduces the tax liability to pay. Tax avoidance is a legal method and it has not been prohibited by any law. Due to these common practices, it has a significant impact on the Indian economy. Due to the sizable amount of money that is typically lost as a result of these practices, the effect of tax evasion and tax avoidance on India's economic growth is an important factor to take into account. Tax evasion results in a decrease in the amount of money the government can bring in, which can result in budget deficits, a reduction in public services, and overall easing of the pace of economic expansion.

TAX

A tax is a legally required fee or charge imposed by municipal, state, and federal governments on individuals and businesses in order to finance vital public services, programmes, and operations. The government's primary source of income is taxes. The levying of taxes is called taxation. The taxes may be imposed on the income and wealth of persons or corporations but the rate of taxes may vary. There are other kinds of taxes like wealth tax, property tax, gift tax, sales tax etc. The tax can be classified into various types on the basis of nature, form, method, aim. The traditional classification of tax is direct tax and indirect tax.

DIRECT & INDIRECT TAX

A direct tax is one that is paid directly to the taxing authority i.e., government by a person or an organization. A direct tax cannot be passed along to another person or organization. The person or organization who is subject to the tax is accountable for making the required payments. A taxpayer may be required to pay a direct tax to the government for a variety of reasons, including real estate taxes, personal property taxes, income taxes, asset taxes, FBT, gift taxes, capital gains taxes, etc.

The example of direct tax is income tax, wealth tax, corporate tax etc.

Income tax It is a tax it is levied on the individuals to pay the tax on the basis of the income earned.

Corporate tax the corporate tax is levied on the profits that are earned by the companies.

Wealth tax is the tax levied on the basis of the wealth of the person.

INDIRECT TAX

An indirect tax is one that is imposed on a person's expenditures that is initially paid by one person but whose burden is ultimately transferred to another person. Excise duty, sales tax, custom duties etc. are examples of indirect taxes. GST replaced all except customs and excise to liquor and petrol in contrast to direct taxes, indirect taxes are typically obtained from the final customer via a middleman. It is then the intermediary's responsibility to forward the tax to the government. Everyone pays the same indirect tax rate, which is independent of an individual's income. In India, the Central Board of Indirect Taxes and Customs (CBIC) is in charge of overseeing indirect taxes.

Goods and service tax, value added tax, customs duty are some examples of indirect tax.

TAX EVASION

In India, most people do not pay their taxes. They attempt to get around this by using illicit methods or by taking advantage of certain tax loopholes in India. The term "tax evasion" refers to the unlawful methods used by individuals, corporations, trusts, and other entities to avoid paying taxes. It involves purposefully lying to tax authorities about the true nature of their business in order to lower or avoid paying taxes by understating their expenses or declaring lower incomes, profits, or gains than they actually made. revenue that would have gone towards social and economic advancement is instead utilized on antisocial activities. All of this is detrimental to the nation's development because it encourages social evils and black money. Additionally, the amount of evasion tax has been determined by chartered accountants and tax attorneys who assist businesses, individuals, and firms in avoiding paying taxes. Evading taxes is a crime in all major nations, with penalties for offenders including fines and confinement.

TAX AVOIDANCE

By using tax avoidance, we satisfy all legal requirements while simultaneously lowering our tax liability; we are not punished or fined for tax avoidance because we are not breaking any laws; rather, we are simply taking advantage of legal loopholes to reduce our tax burden. Tax avoidance is a legal means of reducing our tax liability by taking advantage of lack of provision in the law and it will result in less tax being paid by us. Since tax avoidance entails tax dodging and delays tax liability, it is regarded as immoral. Making adjustments to the accounts so that there are no tax laws broken is one method of tax avoidance. Although it is legal, tax avoidance may occasionally be regarded as fraud.

LITERATURE REVIEW

"IMPACT OF TAX AVOIDANCE AND TAX EVASION IN INDIA- A STUDY":[1]Asia Pacific Journals, By Manjula Bai H**a**thi's paper presents an outline for comprehending the effects of tax evasion and avoidance in India. The government continues to make efforts, but not always successfully, to stop the problem of tax evasion and avoidance, as evidenced by the slowdown in economic growth. Thus, the goal of this study is to identify appropriate solutions for resolving those issues and to overcome them.

---

[1] Manjula Bai H "IMPACT OF TAX AVOIDANCE AND TAX EVASION IN INDIA- A STUDY"10(1)2001ELk Asia Pacific journal Of Finance and Risk Management <https://www.elkjournals.com/MasterAdmin/UploadFolder/Manjula-%20Paper/Manjula-%20Paper.pdf> accessed on 20th nov 2023.

"UNVEILING THE CONSEQUENCES: EXPLORING THE EFFECT OF TAX EVASION AND TAX AVOIDANCE ON INDIA'S ECONOMIC.[2] Progress's Sahi Khushi Sharma. This paper emphasizes the extensive destruction that tax evasion and tax avoidance cause to India's economic growth. It offers indications in support of laying into action practical measures to stop these conducts in order to advance India's sustainable economic development.

IMPACT OF TAX EVASION & AVOIDANCE INDIAN CONTEXT:[3]Mr. Manju, Mr. Sunil Naik. The article focuses on the ideas of tax evasion and avoidance, the causes of evasion, the various methods of tax evasion and avoidance, government's preventive actions, and the tax laws of 2020 and 2021.

Impact of Tax Evasion and Tax Avoidance on Indian Economy:[4]Gupta, Chitraksh This paper offers an understanding of the consequences of tax evasion and avoidance in India. There is still a decline in the rate of economic growth despite all the government's efforts to stop the issue of tax evasion and avoidance. This research paper therefore addresses how to solve those issues and finds a workable solution for them.

The Concept of Tax Evasion and its Impact on National Economy:[5]Anshika Vashist
The author of the article has attempted to provide a general explanation of the subject, outlining its causes, methods used by individuals to avoid paying taxes, and finally, its effects and implications on the national economy. The author has also offered some suggestions for hindering these crimes.

RESEARCH PROBLEM

- ❖ What are the main causes of tax evasion and tax avoidance in tax?
- ❖ How does tax evasion and tax avoidance impact the revenue collection of the Indian government?
- ❖ What measures can the Indian government take to effectively combat tax evasion and tax avoidance?
- ❖ What are the legal policy measures that can be taken to incentivize tax compliance and reduce tax evasion and tax avoidance in India?

[2] Sahi Khushi Sharma "UNVEILING THE CONSEQUENCES: EXPLORING THE EFFECT OF TAX EVASION AND TAX AVOIDANCE ON INDIA'S ECONOMIC PROGRESS "2 (3) Journal of Legal Research and Juridical Sciences <https://jlrjs.com/wp-content/uploads/2023/07/242.-Sahi-1.pdf> accessed on 20th nov 2023.

[3] Mr. Manju & Mr. Sunil Naik "IMPACT OF TAX EVASION & AVOIDANCE: INDIAN CONTEXT ("2021) 8(8) Journal of Emerging Technologies and Innovative Research (JETIR) <https://www.jetir.org/papers/JETIR2108012.pdf> accessed on 21st nov2023.

[4] Gupta, Chitrakshi "Impact of Tax Evasion and Tax Avoidance on Indian Economy" (2022) SSRN. <https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4158909> accessed on 21st nov 2023.

[5]Anshika Vashist "The Concept of Tax Evasion and its Impact on National Economy" <https://www.legalserviceindia.com/legal/article-3712-the-concept-of-tax-evasion-and-its-impact-on-national-economy.html> accessed on 21st nov 2023.

OBJECTIVE OF STUDY

- Aims to analyze the various methods used by the individuals and businesses to evade or avoid taxes, assess the magnitude of revenue loss due to these activities, and evaluate the overall impact of the economy including income inequality, resource allocation and fiscal health etc.
- To understand these practices' impact on the Indian economy is to understand its extent to which these activities occur in the country and the consequences impacted on our economy.
- It explores the potential policy measures and strategies to combat the tax evasion and tax avoidance and the potential benefits of reducing these activities for the economy as a whole.
- Recognizing the country's tax system's weaknesses.

RESEARCH METHODOLOGY

The research methodology used in the paper is strictly doctrinal. The paper is the descriptive analysis of the tax evasion and Tax avoidance -impact on Indian economy. In order to examine the research question and test the hypothesis, data are gathered from secondary sources such as books, journals, articles, media reports, and websites. Additionally, secondary sources will be discussed in order to understand and evaluate the objections raised by the study of this research paper.

SCOPE AND LIMITATION THIS RESEARCH

This study has limitations to the comprehension of tax evasion and avoidance and suggests additional consequences resulting from these actions for the economic development of developing countries such as India. The government's role in combating the issues of tax evasion and avoidance is also covered and analyzed in further research.

REASONS FOR THE TAX EVASION & AVOIDANCE

In both developed and developing nations, there are numerous explanations why people evade and avoid paying taxes. Since developed nations have high levels of tax awareness, the motivations behind tax avoidance and evasion there are different from those in less developed nations and nations in development. A major effect of tax avoidance and evasion is a drop in tax revenue for the government, undermining its integrity. Avoiding and evading taxes leads to lower government revenue, which increases the deficit and forces the government to print money or borrow it more currency, which causes inflation. Examining its circumstances is essential in order to Put forth ideas for reducing or eliminating them. The reasons for the tax evasion and avoidance are as follows:

High tax rates: High tax rates can create an incentive for individuals and businesses to engage in tax avoidance and evasion. When the tax burden is substantial, people naturally look for legal and illegal means to reduce the tax liability that is imposed on them. They also explore the offshore tax havens, trust or complex structures to legally minimize taxes or resort to illegal activities to evade the taxes altogether.

Complexity of tax laws: Tax codes are often intricate and complex, making it easier for individuals and businesses to exploit loopholes or engage in aggressive tax planning. The complexity can create confusion, enabling tax avoidance activities that exploit unclear provisions or mismatches between different tax ways.

Lack of transparency in tax systems: In some cases, there is lack of transparency in tax systems or weak enforcement mechanisms can encourage tax avoidance and evasion. Limited resources for tax authorities, bribery and corruption can undermine their ability to effectively monitor and enforce compliance. This creates an environment where individuals and businesses may feel they can evade taxes without severe consequences.

Globalization and multinational corporations: The globalized economy has led to increased opportunities for multinational corporations to exploit differences in tax laws and regulations across jurisdictions. Creating complex corporate structures, shifting profits to low-tax jurisdictions or engaging in transfer pricing manipulation, multinational corporations can legally reduce their tax liabilities significantly.

Weak tax administration: Inadequate enforcement and lack of resources for tax administration agencies increase the likelihood of tax evasion. Weak audit capabilities, limited monitoring and ineffective penalties fail to deter potential evaders.

Corruption and bribery: widespread corruption and bribery can undermine tax collection efforts. Bribes paid to tax officials can result in lenient treatment on tax matters or even complete exemptions, creating an unfair or non - transparent tax.

Perceived unfairness:

Some individuals may engage in tax evasion and tax avoidance due to perceived unfairness that the tax system is unfair or unjust They may argue that the taxes are not used efficiently or that they are disproportionately burdened compared to others, leading to a mindset of tax resistance.

Informal economy:

Countries that have large informal economies are more susceptible to tax evasion. In these cases, individuals and businesses may conveniently avoid declaring their income or transactions, which leads to a significant loss in tax revenue.

Financial gain and greed:

Tax avoidance and evasion often come down to financial gain and greed. Individuals and businesses seek to maximize their profits by minimizing tax obligations, regardless of the societal impact or ethical considerations. The prospect of retaining a higher share of income or profits can be enticing enough to prompt tax avoidance or evasion activities.

Ineffective tax policies:

Tax policies that do not adequately address the loopholes, exemptions or disparities can inadvertently contribute to tax avoidance or evasion. Poorly designed policies can create incentives for individuals and businesses to engage in aggressive tax planning or exploit the legal gaps.

Regulatory competition:

In a globalized economy, countries often compete to attract investment and businesses by offering competitive tax incentives. This may lead to a "race to the bottom" in which nations cut their tax rates, opening the door for tax evasion.

Strategic tax planning:

Individuals and businesses engage in careful tax planning to minimize them
taxes. This includes strategic decisions such as selecting tax-favorable investments, utilizing tax credits or deductions or structuring their affairs in a manner that reduces their taxable income.

In India, companies seek not to pay or dodge taxation in order to preserve cash for transactions or agreements with government offices and hirelings. Experts advise against paying taxes because of the high rates so as to save revenue for the future. Officials in the political and most of the time, other lawmakers avoid prosecution because their income mostly comes from fixes and illegal techniques. The actions of individual citizens, society norms on the market side, and flaws and deficiencies in the revenue or demand part of tax administration all lead to tax evasion and avoidance.

DIFFERENT WAYS OF TAX EVASION & AVOIDANCE

The following are the most common methods used by individuals and companies in practice with the tax evaders to evade taxes.

Underreporting income: The income is deliberately concealed and some or all of their income is to pay less tax.

Overstating Deductions: Individuals may overstate their deductions by claiming expenses that are not legitimate or exaggerating the value of deductible items. Whereas this includes the inflating business, charitable donations or claiming personal expenses as business expenses.

Offshore Accounts: Tax evaders often set up offshore accounts in countries with tax laws to hide their assets and income. They keep their money in offshore banks, individuals aim to avoid reporting their income to tax authorities.

Using shell companies: Establishing shell companies, which are often fake companies without any real operations, can be used to hide income or underreport. Money funneled through these entities to avoid deduction or manipulate the appearance of their income.

Transfer pricing: Multinational corporations may manipulate transfer pricing by artificially inflating costs in high tax countries and reducing profits in low tax countries. This allows them to shift profits to jurisdictions with lower tax rates, reducing their overall tax liability.

Tax Shelters: High income individuals often invest in tax shelters, such as real estate partnerships or limited partnerships, which generates losses that offset their taxable income. These shelters are designed to exploit the loopholes in tax laws.

Incorporating in tax havens: Incorporating a company in a tax haven jurisdiction such as Bermuda allows individuals to benefit from lower tax rates, minimal reporting requirements and heightened privacy.

Tax incentives and deductions: Legally maximizing deductions, credits and incentives offered by tax laws to lower tax liabilities.

Incorporating in tax- friendly jurisdictions: Incorporating businesses in countries or states with lower tax rates or favorable tax laws.

Charity and philanthropy: Donating to charities, foundations, or social causes to qualify for tax deductions.

Employee stock options: Providing employees with stock options as a form of compensation, which can be taxed at a lower rate than regular stock options as a form of compensation which is subject to a lower tax rate than ordinary income.

International tax planning: Utilizing international structures and treaties to reduce overall tax obligations by taking advantage of varying tax rates and exemptions between countries.

Double tax treaty abuse: Some individuals may exploit double taxation agreements between countries to artificially reduce their tax liability by routing their funds through multiple jurisdictions so they avoid paying taxes in either of the countries.

Paying Bribes: Engaging in corrupt practices to avoid paying taxes or to receive preferential tax treatment.

DIFFERENTIATE BETWEEN TAX EVASION & AVOIDANCE

Tax planning and tax avoidance are very similar in that they are both entirely permissible under the law. It is the taxpayer's expectation to plan their taxes, while the government does not anticipate tax avoidance. The Income Tax Act of 1961, for instance, has some provisions that a taxpayer can most effectively use the deductions allowed by Sections 10 and 80C to minimize his or her tax liability to properly carry out tax planning, including Section 80U, Section 37, etc. Yet, in contrast, an organization moving its intellectual property from India to a nation with lower tax rates is a successful instance of tax evasion.

However, contrary to tax planning and avoidance, tax evasion is totally prohibited by law and is not supported in any way by any government. Tax evasion entails breaking the law and is tantamount to outright theft. One typical instance of tax evasion is cash income that was not disclosed. Discovered hidden during the 2016 demonetization campaign in numerous Indian homes. Money that was made unlawful and was unreported wealth that people had amassed through not paying taxes.

Basis for comparison	**Tax evasion**	**Tax avoidance**
Meaning	Reducing tax liability by using illegal means is known as tax evasion.	Minimization of tax liability by taking such means which does not violate the tax rules is tax avoidance.
Legality	illegal	Legal
Objective	Evade or avoid payment of taxes illegally	Reduce tax obligation while staying within the law.
Methods used	Fraudulent activities, false information	Utilizing legitimate tax provisions and strategies
Compliance	Violates tax laws and reporting requirements	Complies with tax laws and reporting requirements
Consequences	Penalties, fines, legal actions, reputation damage	No legal consequences
Examples	Underreporting income, fabricating expenses.	Utilizing tax incentives, deductions and exemptions.

Actionable steps taken by Government of India to combat problem of Tax Avoidance:

The Government of India has taken several actionable steps to combat the problem of tax avoidance under the Income Tax act 1961 and Finance Act 2015. The following are the steps:

Introduction of General Anti-Avoidance Rules (GAAR): GAAR provisions were introduced in the Finance Act, 2015, to empower tax authorities to deny tax benefits to any arrangement that is deemed to be an impermissible tax avoidance arrangement. Under GAAR, tax authorities are granted the power to determine the legitimacy of tax positions that are overridden by commercial considerations. This means that if a taxpayer engages in transactions or arrangements primarily for the purpose of obtaining tax benefits, rather than for genuine commercial reasons, the tax authorities can disregard such arrangements and tax the taxpayer accordingly.

The implementation of GAAR is aimed at preventing arrangements or transactions that have the sole purpose of avoiding taxes by taking advantage of loopholes in the law. These provisions ensure that taxpayers cannot misuse legal provisions and artificially structure their affairs to avoid tax liability.

The key feature of GAAR is that it empowers tax authorities to invalidate transactions or arrangements that are determined to be abusive or lacking in commercial substance. The tax consequences of such transactions can then be adjusted to prevent tax avoidance. The introduction of GAAR in India is a significant step towards curbing aggressive tax planning and promoting tax compliance. It provides tax authorities with the necessary tools to combat tax avoidance through the misuse of legal provisions and ensures that taxpayers pay their fair share of taxes.

Base Erosion and Profit Shifting (BEPS) Implementing the Action Plan:

India has been actively participating in the BEPS initiative led by the Organization for economic co-operation and development (OECD). The BEPS action plan aims to counter tax avoidance strategies used by multinational companies. India has taken measures to align its domestic legislation with the BEPS recommendations. One of the key objectives of the BEPS action plan is to ensure that profits are taxed where economic activities generating the profits are conducted and where value is created. To achieve this, India has introduced several measures to prevent profit shifting and base erosion.

Firstly, India has implemented country-by-country reporting (CyBC) requirements for multinational companies. Under these requirements, multinational companies are required to provide detailed information on their global activities, including their profits, taxes paid, and economic activities in each country. This helps tax authorities to gain better insights into the operations of multinational companies and identify any potential tax avoidance strategies. Secondly, India has implemented the Multilateral Instrument (MLI) developed by the OECD.

Strengthening Transfer Pricing Regulations: Transfer pricing regulations have been strengthened to ensure that transactions between associated enterprises are conducted to ensure at arm's length prices. The government has introduced the concept of range to determine the arm's length price and more stringent documentation requirements have been imposed on taxpayers. The purpose of these strengthened regulations is to ensure that transactions between associated enterprises are conducted at arm's length prices. This means that the prices charged for the goods, services, or intellectual property transferred between the entities should be similar to what would be charged between unrelated parties in an open market.

By implementing range concepts and imposing stricter documentation requirements, the government aims to prevent tax avoidance and profit shifting through transfer pricing manipulation. This helps to ensure that companies are not unfairly reducing their tax liabilities by artificially inflating or deflating prices in transactions with associated enterprises.

Overall, strengthening transfer pricing regulations helps to promote fairness and transparency in international transactions between associated enterprises. It reduces the risk of tax avoidance and ensures that businesses are paying their fair share of taxes in each jurisdiction where they operate.

Introduction of country-by -country reporting (CBCR): Under the Finance Act 2016, India implemented CBCR, requiring multinational companies to furnish details of income, taxes paid, and economic activities in each country of their operations. This measure aims to curb base erosion and profit shifting by providing enhanced transparency allowing tax authorities to gain a better understanding of multinational companies' operations across different jurisdictions. By requiring detailed information about income, taxes paid, and economic activities, tax authorities can identify any potential tax avoidance strategies used by these companies.

This information is crucial in determining whether profits are being shifted to low-tax jurisdictions, resulting in a loss of tax revenue for the countries where the economic activities actually occur. The implementation of CBCR in India is part of a global effort to combat. This measure serves as a deterrent for companies engaging in aggressive tax planning and profit shifting practices, as they are now required to disclose detailed information about their global operations.

The transparency provided by CBCR also benefits other stakeholders, such as investors and civil society. Investors can make more informed decisions by understanding a company's global tax practices and the potential risks associated with tax avoidance.

Exchange of Information: India has strengthened its information exchange mechanism by signing various Double Taxation Avoidance Agreements (DTAAs) and Tax information Exchange Agreements (TIEAs)with other countries. These agreements facilitate the exchange of tax - related information between jurisdictions making it difficult for taxpayers to hide their assets of their income. Double Taxation Avoidance Agreements are bilateral agreements signed between two countries to avoid the situation of double taxation. Under these agreements, both countries agree on rules for the allocation of tax jurisdiction over various types of income, such as income from business, interest, royalties and capital genistas provide certainty to taxpayers about their tax obligations in both countries and reduce the potential burden of double taxation. They establish mechanisms for resolving any disputes that may arise between the tax authorities of the two countries.

Widening the tax base: The government has taken steps to increase the tax base by promoting digital transactions, implementing the Goods and Services Tax (GST), and encouraging voluntary compliance through campaigns like the Black Money Act. This is done to generate more revenue for the government and reduce the fiscal deficit. Several measures have been taken in India to achieve this objective.

Promoting digital transactions: The government has been actively promoting digital transactions as a way to widen the tax base. By encouraging people to use digital payment methods such as credit/debit cards, mobile wallets, and online banking, the government can track transactions more easily and reduce the scope for tax evasion. It also reduces the reliance on cash transactions, which are often unrecorded and can lead to tax evasion.

Implementing the Goods and Services Tax (GST): The introduction of GST in India has been one of the most significant steps towards widening the tax base. GST replaced multiple indirect taxes levied by the central and state governments, bringing in a uniform tax structure. It subsumed various taxes like excise duty, service tax, value-added tax (VAT), etc., and expanded the tax base by including more businesses and sectors under its purview. The GST implementation helped eliminate tax cascading, reduce corruption, and bring several businesses into the formal tax system.

Encouraging voluntary compliance: The government has undertaken various campaigns and initiatives to encourage voluntary tax compliance. One such initiative is the Black Money (Undisclosed Foreign Income and Assets) and Imposition of Tax Act. This act aims to tackle black money, undisclosed foreign assets, and income earned from them. It offers a compliance mechanism for those who failed to disclose such assets or income in the past to come forward voluntarily and declare them, with payment of appropriate taxes and penalties.

Impact of the tax evasion and tax avoidance on National economy

Loss of Government Revenue: Tax evasion and avoidance lead to a reduction in the amount of tax revenue collected by the government. This loss of revenue can negatively affect government budgets, leading to reduced funding for essential public services such as healthcare, education, infrastructure, and social welfare programs.

Increased Budget Deficit: The loss of tax revenue due to evasion and avoidance can contribute to a larger budget deficit. This, in turn, may result in higher government borrowing, increased public debt, and potential economic instability.

Inequality and Unfairness: Tax evasion and avoidance exacerbate income inequality and unfairness within a society. Those who can afford to engage in these activities often end up paying lower effective tax rates compared to individuals who cannot exploit such loopholes.

Distorted Market Economy: Tax evasion and avoidance can distort the functioning of the market economy. When some businesses or individuals can avoid taxes, they gain a competitive advantage over their counterparts who operate within the legal framework. This can create unfair competition, hinder market efficiency, and lead to market inefficiencies.

Decreased Investor Confidence: Widespread tax evasion and avoidance can erode investor confidence in a country's economic system. This is particularly true for foreign investors who may perceive a lack of legal and fiscal stability. The resulting decrease in foreign direct investment affects economic growth and job creation.

Higher Tax Burden on Honest Taxpayers: When individuals and businesses evade or avoid taxes, the burden of funding public expenditures falls more heavily on honest taxpayers. Governments may respond by increasing tax rates or introducing new taxes to compensate for lost revenue, which can place an additional burden on those who already pay their taxes honestly.

Lack of Fiscal Space: Tax evasion and avoidance can limit a government's ability to invest in infrastructure, public services, and other productive sectors. This limits the government's capacity to stimulate economic growth, reduce unemployment, and improve the overall standard of living for its citizens.

LEGAL PROVISIONS RELATED TO TAX EVASION & AVOIDANCE UNDER INCOME TAX ACT 1961

Section 271H:[6] It deals with the late filing of income tax returns, which is considered a form of tax evasion. This is a punishable offense under the Income Tax Act, 1961, with a penalty ranging from Rs. 10,000 to Rs. 100,000 for the taxpayer.

Section 270A:[7] It addresses the concealment of income from the tax department, which is a serious offense in tax evasion. In order to prove this offense, the assessing officer must be convinced that the taxpayer has hidden their income.

[6] Income Tax Act 1961, s 271H.
[7] Income Tax Act 1961, s 270 A.

Section 271B:[8] It pertains to individuals who fail to get their accounts audited as required under section 44AB of the Income Tax Act, 1961.

Section 234E:[9] It deals with non-compliance with TDS rules. If a business or institution fails to submit tax deducted at source or tax collected at source (TCS) returns on time, they are liable to pay a penalty of Rs. 200 per day, with the penalty not exceeding the total TDS amount.

Under Section 276C:[10] The **individuals** intentionally evading taxes or understating their income by more than Rs. 25 lakhs can face imprisonment for a minimum of six months up to seven years, along with a fine. Providing false information, including PAN data, when filing an income tax return is illegal.

Section 139A:[11] It addresses the illegality of providing false information, including PAN data, when filing an income tax return. All tax deductions, including employers, require PAN card IDs for proper TDS collection.

PENALTIES

The Income Tax Act in India specifies penalties for taxpayers who commit various acts of omission, deliberate neglect, and purposeful tax evasion in a given financial year. In addition, penalties are also outlined for corporations that fail to maintain the necessary documentation and comply with regulatory requirements during a financial year.

Examples:

A) Section 270A of the act holds taxpayers accountable for penalties if they attempt to reduce their tax liability by underreporting income. In such cases, the penalty can be as high as 200% of the tax payable on the unreported income.

B) Section 271A imposes a penalty of Rs. 25000 on a taxpayer who fails to maintain proper bookkeeping as required by section 44AA.

C) Assessing officers can impose penalties on taxpayers for defaulting on tax payments, as stipulated in section 220 (1) and 221 (1) of the income tax acts.

[8] Income Tax Act 1961, s 271 B.
[9] Income Tax Act 1961, s 234E.
[10] Income Tax Act 1961, s 276 C.
[11] Income Tax Act 1961, s 139A.

PENALTIES FOR TAX EVASION

Criminal Offense: Tax evasion is considered a criminal offense in many jurisdictions. It is not simply a civil matter but can lead to criminal charges, fines, and imprisonment.

Legal Provisions: Legal provisions related to tax evasion may include the following:
a. Criminal Charges: Tax evasion can result in criminal charges against the individual or entity involved. The specific charges may vary, but common ones include fraud, false statements, and tax evasion itself.

b. Penalties and Fines: If found guilty, tax evaders may face significant penalties and fines. These can be based on a percentage of the evaded tax amount or can be a fixed amount specified in the tax laws.

c. Imprisonment: In some cases, tax evasion can lead to imprisonment. The length of imprisonment depends on the severity of the offense and the tax laws of the jurisdiction.

d. Investigation and Audits: Tax authorities have the power to investigate and audit individuals or entities suspected of tax evasion. They can request financial records, conduct interviews, and scrutinize tax returns to assess whether tax evasion has occurred.

e. Asset Seizure: Tax authorities may also have the power to seize assets and properties of individuals or entities involved in tax evasion. This is done to recover the evaded taxes or to compensate for the unpaid amounts.

PENALTY FOR TAX AVOIDANCE IN INDIA

Penalties for tax avoidance in India can vary depending on the specific circumstances and the amount of tax evaded. The Income Tax Act, 1961, outlines several provisions and penalties for tax avoidance.

Penalty for underreporting of income: Underreporting of income can result in a penalty equal to 50% of the tax payable on the underreported income.

Penalty for concealing income or furnishing incorrect information: Concealing income or furnishing incorrect information can result in a penalty ranging from 100% to 300% of the tax sought to be evaded.

Penalty for failure to maintain proper books of account: If a taxpayer fails to maintain proper books of account, they can be liable to pay a penalty of up to 2% of the average total sales or turnover.

Penalty for failure to comply with tax provisions: Non-compliance with various tax provisions, such as not filing tax returns or not paying tax dues, can result in a penalty of up to Rs. 10,000.

Prosecution: In severe cases of tax evasion, criminal prosecution may be initiated, which can lead to imprisonment for a term ranging from three months to seven years, along with a fine.

CASE LAWS:

Vodafone International holding vs Union of India SC 2012[12]

It's a landmark case of tax avoidance. The Supreme Court of India recently delivered a significant ruling in which it nullified the Bombay High Court's demand for a capital gain tax of INR 12,000 crore. Vodafone Holding and Hutchison Telecommunication Limited, both classified as non-resident entities for tax purposes, were absolved of this financial burden. The court established that the Indian revenue authority lacks the authority to levy taxes on offshore transactions involving a non-resident company acquiring controlling interest in an Indian resident company. This ruling addresses a blatant case of tax avoidance.

Commissioner Of Income Tax Vs Provident Investment Co. Ltd ,1957[13]

The court ruled that in cases where a company has transferred ownership through a sale, it would bear the responsibility, but in situations where it has voluntarily given up its authority in exchange for compensation, this does not qualify as a transfer under Section 12B. As a result, the company's exemption from taxation is legally permissible, although it may be viewed as morally questionable.

Calcutta Chromotype Ltd. V. Collector of C. Ex., Calcutta., 1998(99) E.L.T 202(S.C)[14].

The Supreme Court, with great concern, has stated that the use of deceptive tactics and manipulative strategies for the purpose of evading taxes, also known as colorable devices, should not be considered a legitimate part of tax planning. Such dubious methods that aim to avoid tax payment on actual income cannot be admired or recognized as clever actions endorsed by a wise individual. Instead, they should be strongly condemned and met with severe penalties.

RECOMMENDATIONS:

Strengthen Tax Administration: The government should focus on strengthening its tax administration by investing in technology and resources to improve the efficiency of tax collection, monitoring, and compliance mechanisms. This includes utilizing data analytics, expanding the tax base, and adopting advanced systems to detect and deter tax evasion and avoidance.

---

[12] Vodafone International Holding vs Union of India 20 Jan, SC 2012.

[13] Commissioner Of Income Tax vs Provident Investment Co. Ltd, 1957 SCR1141.

[14] Calcutta Chromotype Ltd. V. Collector of C. Ex., Calcutta., 1998(99) E.L.T 202(S.C).

Simplify Tax Laws: There is a need to simplify and rationalize the tax laws and regulations to minimize loopholes and ambiguities that facilitate tax evasion and avoidance. The introduction of a unified tax code, with clear and transparent rules, can reduce opportunities for tax manipulation and increase compliance**.**

Enhance International Cooperation: Given the global nature of tax evasion and avoidance, it is crucial for the Indian government to enhance international cooperation in information exchange and tax enforcement. Strengthening bilateral and multilateral agreements with other countries can help in tracing and recovering offshore assets and income.

Increase Awareness and Education: The government should undertake awareness campaigns to educate citizens about the importance of paying taxes and the consequences of tax evasion and avoidance. This can help in changing societal attitudes towards tax compliance and foster a culture of tax morality.

Reward and Whistleblower Protection: Offering incentives and rewards to taxpayers who report instances of tax evasion can encourage voluntary compliance and help uncover hidden assets and income. Whistleblower protection mechanisms should also be established to protect identity and ensure the safety of those reporting tax evasion.

Promote a Cashless Economy: Encouraging digital payments and reducing cash transactions can help in curbing tax evasion and improving tax compliance. This can be achieved through the promotion of electronic payment systems, demonetization measures, and the establishment of a robust digital infrastructure**.**

By implementing these recommendations, the Indian government can effectively address the issue of tax evasion and tax avoidance resulting in increased tax revenue, improved fiscal stability and greater trust in the taxation system ultimately benefiting the overall Indian economy.

CONCLUSION:

Tax evasion and tax avoidance have significant negative impacts on the Indian economy. These practices lead to a loss of revenue for the government, hindering its ability to fund essential public services such as healthcare, education, and infrastructure development. This loss of revenue also exacerbates income inequality, as the burden of taxation falls more heavily on honest taxpayers. Moreover, tax evasion and avoidance undermine the integrity of the tax system, eroding public trust and confidence in the government. This can harm the overall business environment by discouraging domestic and foreign investment, as potential investors may view the tax system as unfair and unreliable.

Additionally, these practices foster a culture of noncompliance and disregard for the rule of law. When individuals and businesses evade or avoid taxes, they are essentially shifting the burden onto honest taxpayers, exacerbating the economic inequalities prevalent in the country. Furthermore, tax evasion and avoidance impede economic growth by limiting the government's ability to invest in key sectors and infrastructure projects. Adequate funding is crucial for these initiatives, and the lack of revenue due to tax evasion and avoidance hampers progress in these areas.

To address these issues, the Indian government should take proactive steps to strengthen the tax administration system, including streamlining tax laws, improving enforcement capacity, and implementing stricter penalties for tax evaders. Additionally, promoting transparency and encouraging voluntary compliance through effective taxpayer education programs could also contribute to mitigating the negative effects of tax evasion and avoidance on the Indian economy. Ultimately, combating tax evasion and avoidance is not only essential for the sustained development of the Indian economy but also crucial for ensuring fairness, equal distribution of burden, and public trust in the tax system. By addressing these issues, the government can increase revenue collection, channel funds towards vital sectors, and foster a conducive environment for economic growth and investment.