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IDS BONANZA



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Evil Consequences of Tax Avoidance

1. The Supreme Court in *Mc Dowell & Co. Ltd. v. CTO* [1985] 154 ITR 148/22 *Taxman 11* made a reference to the evil consequences of tax avoidance in a Welfare State like India with following pointers (Pg 160-161):–

"The evil consequences of tax avoidance are manifold. First, there is substantial loss of much needed public revenue, particularly in a welfare state like ours. Next, there is the serious disturbance caused to the economy of the country by the piling up of mountains of black money, directly causing inflation. Then there is "the large hidden loss" to the community (as pointed out by Master Sheatcroft in 18 Modern Law Review 209) by some of the best brains in the country being involved in the perpetual war waged between the tax-avoider and his expert team of advisers, lawyers and accountants on the one side and the tax-gatherer and his perhaps not so skillful advisers on the other side. Then again there is the "sense of injustice and inequality which tax avoidance arouses in the breasts of those who are unwilling or unable to profit by it". Last, but not the least is the ethics (to be precise, the lack of it) of transferring the burden of tax liability to the shoulders of the guideless, good citizens from those of the "artful dodgers". It may, indeed, be difficult for lesser mortals to attain the state of mind of Mr. Justice Holmes, who said, "Taxes are what we pay for a civilized society. I like to pay taxes. With them I buy civilization." But, surely, it is high time for the judiciary in India too to part its ways from the principle of Westminster and the alluring logic of tax avoidance. We now live in a welfare State whose financial needs, if backed by the law, have to be respected and met. We must recognise that there is behind taxation laws as much moral sanction as behind any other welfare legislation and it is a pretence to say that avoidance of taxation is not unethical and that it stands on no less a moral plane than honest payment of taxation. In our view, the proper way to construe a taxing statute, while considering a device to avoid tax, is not to ask whether the provisions should be construed literally or liberally, nor whether the transaction is not unreal and not prohibited by the statute, but whether the transaction is a device to avoid tax, and whether the transaction is such that the judicial process may accord its approval to it. A hint of this approach is to be found in the judgment of Desai J. in *Wood Polymer Ltd., In re* [1977] 47 Comp. Cass. 597 (Guj.), where the learned judge refused to accord sanction to the amalgamation of companies as it would lead to avoidance of tax."

IDS - A Bonanza

2. One of the reasons pointed out by the Apex Court for tax avoidance is the occupation of the best brains in the country helping the tax avoider. The Income Declaration Scheme 2016 or IDS Scheme offer a Bonanza to the tax avoiders to revisit their accounts and straighten them by paying taxes equivalent to 45% of the undisclosed income without any questions being asked. In other words the scheme offers one time

opportunity to clean up tax records. It is thus onerous duty of the best brains now to rechristen their role and to shoulder on the national cause and to further educate the tax avoiders of the advantages offered under the IDS scheme equivalent to a bonanza.

Pitfalls of Not Availing IDS

3. And just in case one fails to avail the scheme he would end up coughing more than three times the taxes on undisclosed income given the present stiff tax laws and penalty scheme. In their [Circular No. 25 dated 30th June 2016](#) a caution notice is issued by the Board stating that the Income-tax Department is in receipt of large volume of information from various sources such as registrars of property, banks, financial institutions, stock exchanges, tax deductors etc. The Department has launched a comprehensive data-mining and compliance management programme in the form of 'Project Insight' which will generate a large volume of reliable information about financial transactions undertaken by taxpayers and the relevant year in which the transaction was undertaken. More so section 197 (c) of the Finance Act, 2016 in so many words also caution out that in case a person do not make a declaration of undisclosed income now he may then run a risk of receipt of formal notice on the basis of information drawn from 'Project Insight'. Not to be missed is the fact that in such an event the entire income would be deemed as income of the year in which such information is acted upon by issue of notice u/s [142/143\(2\)/148/153A/153C](#).

For instance a person may have invested into a piece of land of say Rs. 10,00,000/- out of undisclosed income in financial year 2000-01. And assuming that the value of such plot has risen to Rs. 15,00,000/- as on 1.6.2016. In one situation such individual could declare value of such plot at Rs. 15,00,000/- which is higher than the cost and pay a tax at 45% on such amount by availing the IDS. Now in the event he does not avail of the scheme and subsequently if such data is found out then he would be taxable on the market value of such plot in the year in which the notice is received. If suppose the value has gone up to Rs. 50,00,000/- then he would end up paying tax on Rs. 50 lacs. Besides he would end up paying interest for 15 years equivalent to 180% of the amount of tax besides a penalty of 200% of tax. And that could be complete disaster for someone who misses to avail of this bonanza.

4. Advantages of IDS

- (1) There is no need to disclose the source of income or source of investment in undisclosed asset at all. One just needs to write down the nature of undisclosed income earned in respective year such as rent, business receipts, miscellaneous incomes or the nature of undeclared asset held such as cash in hand, securities, land residential or commercial property such as shop, office, agricultural land, jewellery, car, sundry creditors, share capital, unsecured loan, expense payable etc. A list of items of undisclosed income or undisclosed assets may be appended to the form of declaration.
- (2) The second advantage is that once the declarant pay tax he may end up getting depreciation should such asset is put to use for business purpose. Else one can sell the asset in future and realize payment by cheque which money one can reinvest and get tax breaks. Even the declarant can gift such assets to their children any time later.
- (3) There is zero risk of a declaration. The transaction under declaration will not be investigated in future by anyone. For instance if the declarant has received say Rs.5 lacs on money in cash on sale transaction of declared property he may declare cash amount of Rs. 5 lacs and pay tax at 2.25 lacs tax and unspent sum out of 2.75 lacs he may deposit in the bank. No questions will be asked on such deposit.
- (4) A person can declare bogus purchases, bogus creditors. A person can declare the value of such purchase even if the liability is squared up in the books and pay tax on such transaction booking. Having paid such tax he may introduce the remaining 55 % of amount declared in the books as his capital and deposit cash in the bank. In case of outstanding creditors scenario those can be transferred to capital account in the books
- (5) A company may declare bogus share capital, cash credits, loans, creditors, advances received,

share capital, payables etc. Such amounts have to be transferred to promoters account subsequently.

- (6) There is immunity from prosecution to the declarant as against which a person who does not avail of the scheme for his undisclosed income or assets would have a prosecution risk all his life
- (7) A person can make a declaration even when a scrutiny (limited or otherwise) notice has been issued in his case provided the date of issue is subsequent to 31st May 2016.
- (8) *Vide Circular No. 28, dated 18th August 2016* it has been clarified the income declared for an earlier assessment year can be taken into account to explain the transactions in subsequent year provided there is a nexus between the income declared and the transactions of the subsequent assessment year. For instance a declaration in terms of bogus credit purchase made in earlier year may hold good to defend bogus creditor balance corresponding to such purchase in subsequent year.
- (9) Further *Vide Circular No. 32 dated 1.9.2016* it is assured that the declaration once accepted by the department will become sacrosanct and cannot even be questioned by any survey team or in the course of any search action tomorrow.
- (10) The scheme provides flexibility to the declarant in the matter of payment of amount of tax, penalty and surcharge on the declaration made. Such amounts can be paid in three installments:
 - (i) not less than twenty-five per cent. of such tax, surcharge and penalty by the 30th day of November, 2016,
 - (ii) not less than fifty per cent. of such tax, surcharge and penalty as reduced by the amount paid under clause (i) by the 31st day of March, 2017;
 - (iii) the whole amount payable under section 184 and 185 as reduced by the amounts paid under clause (i) and (ii) above by the 30th day of September, 2017.

Conclusion

5. Ordinarily there can be no penalty or prosecution under the law when a person declare income as income from other sources without citing the source of such income as long as there is no allegation against him that any income was sought to be held back or was not disclosed by him in the returns *vide Patna Guinea House v. CIT [2000] 243 ITR 274/[2002] 123 Taxman 883 (Pat.)*. IDS, 2016 however offers substantial waivers from penalty and complete waiver from prosecution even with reference to income not disclosed by the declarant in its return of income and this certainly is a very big bonanza for declarants. Thus looking at the advantages of the scheme it is wise to avail this bonanza by those who have not filed their taxes properly in the past. Even when one go for settlement of his case he has to explain the source of income along with the declaration. The IDS 2016 does not seek any kind of source explanation from the declarant. All it requires is a correct and complete declaration of undisclosed income or undisclosed asset, as the case may be. The greatest pitfall of not going by the scheme is the power to the Income tax Officer to consider the value of the asset acquired out of undisclosed income at their market value of current date meaning higher tax burden upon the non-declarant and loss of indexation benefits on future sell-off of such asset.

