



International Journal of Financial Management and Economics

P-ISSN: 2617-9210
E-ISSN: 2617-9229
IJFME 2021; 4(1): 81-84
Received: 20-11-2020
Accepted: 23-12-2020

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Evasion and avoidance of income tax in India

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Abstract

Revenue plays a very important role in the development of any country especially in developing country like India. Direct taxes have a important part in the revenue of the Central Government. The contribution of the Income Tax is greater than any other direct taxes in the Government revenue. Complex nature of our law relating to taxes, high tax rate, defective administrative machinery and increasing tax liability create the problem of Evasion and Avoidance of Income Tax in India. Income tax has been effective in India since 1860. Indian Income Tax is lacking in simplicity. Because of its complicated nature, tax-payer find it easy and possible to avoid tax by legal ways. The object of the present study is to know the causes of evasion and avoidance of Income Tax in India, so as to take remedial measures so that this evil may be abolished, Government may be increased and creation of black money, which is a curse to the economy, may be checked.

Keywords: Tax evasion, taxation system, pan card, income

Introduction

Tax evasion is the deliberate omission to pay taxes legally. It is an escapement by the elimination of reduction of one's correct and proper tax by fraudulent means. It is also done in outright breach of the statutory provisions, in other words, it denotes downright defrauding of revenue through illegal acts and deliberate suppression or falsification of the facts relating to one's true tax liability, briefly stated: the reduction of taxes by illegal and improper means constitutes tax evasion. On the contrary tax avoidance is reduction of taxes in just the other way i.e., by lawful means recognised and deliberately permitted by law.

The avoidance is the elimination or reduction of taxes through lawful means. It streams through the course of our entire tax structure. Webster has rightly defined "Avoidance" as the act of keeping away from the keeping clear of taxes. As to the nature of tax avoidance there is a difference of opinion. There are those who maintain that tax avoidance is both immoral as well as unlawful. Contrary to these, there are others who do not smell any foul odour in tax avoidance and regard it as perfectly moral and lawful.

Thus to say that Tax Avoidance is immoral is sanctimonious nonsense. Tax Avoidance unlike evasion is not a crime but a right. A taxpayer who, because of neglect or ignorance does not minimise tax liability to the full extent permissible by law, is, in effect, paying more than his fair share of the price of the civilised society.

In other words, evasion implies a deliberate attempt on the part of the taxpayer, at distortion of facts and infringement of the letter and spirit of the law after the liability to tax is incurred. Avoidance on the other hand, is the result of deliberate pre-planning before the liability to tax is actually incurred. As the evasion is resorted to by way of deceit, dodging, prevarication, it may be regarded as immoral and fraudulent.

Tax evasion is illegal action in which an individual or company avoid paying tax liability. It involves hiding or false income, without proof of inflating deductions, not reporting cash transaction etc. Tax evasion is serious offense comes under criminal charges and substantial penalties. It is an illegal act and attracts penalty and proceedings against the person. It is a deliberate omission of income on a tax return, the non-payment of taxes owed or not filing a tax return altogether, to avoid having to pay taxes to the government. It can be done by declaring less income or profits than the amount actually earned. It is an unlawful attempt to minimize tax liability through fraudulent techniques to circumvent tax laws.

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Some common practices of tax avoidance schemes which are also permissible by law are as under:

1. Tax avoidance through Charitable Trusts
2. Tax avoidance through formation of Private Limited Company
3. Tax avoidance through partition of H.U.F.
4. Tax avoidance through Tax Planning: The government wants that people should save a considerable part of their income by investing in various securities and deposit schemes. Similarly, the government wants people to earn money through various specified securities not only this but the government wants that people should spend some of their money in several specified heads of expenditure. With a view, the Act provides many such provisions through which these may be channelised. The whole of Section 80 has been contracted to achieve this goal. Right from Section 80C to Section 80U a variety of encouragements for savings, incomes and expenses have been provided. These sections encourage tax avoidance through specified income and expenses.
5. Tax Avoidance through Deemed Incomes.
6. Tax avoidance through Formation of Firms

Penalty for tax evasion in India

The penalty for tax evasion can depend on the fraud committed and the extent of tax unpaid. Here are some situations and the subsequent penalties levied in case of each:

Proving incorrect pan card number or hiding the pan card number

Most employers ask for the employees' pan card number at the time of employment. This information is used while deducting TDS or the tax deducted at source from the employee's salary. The penalty for two scenarios involving a pan card is:

Hiding the pan card number

In the absence of a pan card number, the employer will deduct 20% TDS as opposed to 10% TDS.

Providing an incorrect pan card number

In case of an incorrect pan card number, one will have to pay a penalty of Rs. 10,000.

Concealing or misreporting your Income

As per Section 271(C) of the Income Tax Act of 1961, in case of hiding or understating the income, the penalty can be anywhere between 10% and 200% of the amount of tax that was due but not paid. The percentage is decided as:

- A penalty of 10% on the previous year's income that is hidden or understated is levied if the taxpayer owns up to the undisclosed income and declares it. Interest may also be charged here.
- A penalty of 50% on the amount of income that is hidden or understated is levied if the reason behind the under-reporting was a bona fide mistake. This refers to a genuine mistake that is not committed with an aim to evade tax.
- A penalty of 200% on the amount of income that is hidden or understated is levied if the mistake was

intentionally made to evade tax. This is also known as a mala fide mistake.

Not complying with TDS regulations

For businesses or employers who deduct and collect tax at source, having a tax deduction account number (TAN) is vital. Not having a TAN can result in a penalty of ₹10,000. There are two kinds of frauds that can be committed in this case:

Not collecting tax at source

In this case, the penalty is the same as the tax that was not deducted at source.

Not filing a TDS return

Just like income tax returns, there is also a due date for filing TDS returns. If the TDS return is not filed within the stipulated time, the taxpayer has to pay tax for every day after the due tax till the time the entire payment is made. The penalty, in this case, can start from ₹10,000 and go up to ₹1,00,000.

Failure to comply with a demand notice

The income tax (IT) department may issue a demand notice if there are inconsistencies found in the income tax return. If this happens, the IT department issues a demand notice stating the amount of tax still owed. The taxpayer is offered 30 days to respond to the demand notice from the day of receiving the document. A failure to respond and pay the tax due can result in a penalty.

Not paying tax as per self-assessment

Failure to pay tax as per self-assessment is considered to be tax fraud under Section 140A (1). In such a case, the assessing officer can levy a penalty up to the total amount of tax owed to the government. However, if there is a valid reason for not paying tax as per self-assessment, the assessing officer may waive off the penalty.

Not getting books of accounts audited

If an organization does not get itself audited or does not submit an audit report, they have to pay a penalty of ₹1.5 lakhs or 0.5% of their sales turnover, whichever is more. In addition to this, if the taxpayer does not provide a report from an accountant as mandated, they have to pay a penalty of at least ₹1 lakh or more.

Tax evasion: Major threat to economic growth & development

Loss of revenue for government

Many times, the Indian Government has failed to collect the estimated amount of tax from the people of our country and this money goes to the black money driven underground economy.

Uncontrollable inflation

When black money is out in the market, the amount of money in the system is higher than the Government expects, thus causing the prices of commodities to increase to a level beyond normal.

Leads to mass poverty

The distribution of wealth and income in our country has been severely affected by the growth of underground economy. Tax evasion leads to poor standards of living of the rural masses and the people BPL as the government cannot undertake welfare measures at the national level. It also brings disequilibrium in the economic condition of the country resulting in the rich becoming richer and the poor becoming poorer.

Lack of technology

Due to the existence of black money, India is facing the problem of shortage of capital. This has the direct impact on the up gradation of technology in all sectors. The major reason behind such backwardness is the parallel economy.

Corruption

While corruption creates black money in the economy, it can also be a result of the growing underground market.

Inflated real estate

Generally, people involved in black money market are always ready to pay more for a piece of land as this helps in converting their coloured money to legal money.

Increase in the tax rates

Due to tax evasion of majority of the rich population, the government is forced to increase the tax rates every year for increasing its revenue which results in increased tax burden of those who pay taxes promptly. Majority of the developmental activities do not take place due to tax evasion and avoidance.

India's Reputation

Black money has resulted in transfer of funds from India to foreign countries which decrease country's reputation globally.

Limitations of Indian tax structure which result in tax evasion**High rate of taxation**

High rate of taxation cause a burden to tax payer. So, they find ways to avoid tax.

Failure to curb bribery

There should be adequate system to curb bribery and corruption among officials. They help taxpayers to avoid tax by taking an agreed share of profit out of evaded tax.

Lack of simplified procedures

Tax structure in India is complex and people find it hard to go to different departments for a single matter.

Complex tax laws and loopholes to avoid tax in laws

Indian tax law is complex. In the same law, people find provisions to escape from tax liability.

Lack of organized and systematic Administration structure.**Frequent changes in Government and Political instability**

Frequent changes and political instability is another reason

of non-implementation of well-defined tax system. Different governments implement different tax system and it becomes difficult to follow.

Frequent changes in tax policies

Tax policies in India are changed frequently by government. It creates confusion among tax payers and officials about the relevant provisions.

Deficiencies in implementing penalty provisions.**Best ways to avoid tax evasion**

1. Reducing tax rates.
2. Make more simplified laws and simplified system.
3. Design a well-organized tax administration structure.
4. Strengthen anti-corruption policies.
5. Increase awareness among taxpayers by conducting seminars, conferences and through media.
6. Design a permanent tax structure.
7. Ensure the political changes do not affect well defined tax structure. Make tax administration more independent and autonomous without losing final control of Government.
8. Audit, tax collection, depositing and filing provisions to be more strengthened and updated.
9. Make penalty provisions stronger and avoid its non-implementation.
10. Encourage taxpayers to pay tax by more friendly schemes.
11. Give relief provisions to huge tax payers.

Tax evasion creates a big problem of Black Money in the country. The present tax structure of India is such that every assessee pays least-tax to the government. This is the cardinal cause and source of black money. The problem of black money is just like tuberculosis, which explodes in the society by its bacteria, remanding the lives of millions. Black -Money also crops-up in the society tuberculosis. The whole society is exposed to its impact, because of economic, social and political interests are so correlated that one cannot be separated from the other.

It is very difficult to give any date of origin of black-money in India. At the most historic account of the origin can be given. The philosophy of black-money is very plain and simple. It is undoubted truth that nobody wants to grow rich in the world, but everybody wants to be richer than others. This is in the root of origin of black-money. Nobody can grow rich by fair means because fair and judicious distribution of national dividend (net Income) leaves nothing with the distributor except his own share in the income, but he is honestly entitled to get his own share, because he has rendered his services in the earning the income. If there remains any surplus after the distribution of income to factors of production that cannot be judicious surplus. This dishonest act of the entrepreneur (employer of other factors of production) is responsible for the origin of black-money in the society. The human nature of growing richer than other is not something of recent origin. It is as old as men's civilization.

Causes of black-money

It is the subject of every one's anxiety as what factors contribute to the origin of black-money. The views

experienced by thinkers and experts of the subject are commendable to narrate the causes of origin of black-money. A few of the causes of black-money may be put as below:

1. High Rates of Taxation
2. Price Control and Licencing policy
3. Donation to Political Parties
4. Smuggling from neighbouring countries
5. Ineffective Taxation Laws
6. Moral Degradation
7. Sky-touching Prices
8. Corrupt Trade-Structure

Impact of black money

It is an accepted phenomenon that black money is responsible for all ills of Indian economy. However, it is very difficult, if not impossible, task to assess the impact of black-money on the society. Majority of people holds the view that the black-money is found with the industrialists and businessmen only, but it is a very wrong view. Unless the Political leaders, the bureaucrats and the businessmen are not in collusion, black-money cannot develop. It is a myth to say that the impact of black-money is always injurious. If black-money is utilised in productive avenues, it stimulates the pace of economic development in the country, but when it is utilised for excessive consumption, it results in increase of prices of goods and services. The economic effects of black-money are always injurious. Black-money increases social injustice. It widens the disparity between rich and poor. It makes an honest man to live in pauper, while the corrupt, dishonest and anti-social people grow rich, command power, dominate others, exploit the poor and terrorise the entire society. On no ethical ground, norms of piety and humanity, black-money can be called a good thing to the society.

Effects of Evasion and Avoidance of Income Tax on Indian Economy

The economic effects may be both beneficial as well as injurious to the economy as a whole.

1. At the very outset, it may be stated that tax avoidance through tax-planning, minimises the tax liability of the tax-payer and provides him economic relief.
2. Tax avoidance provides incentives to increase production to certain manufacturers, especially as export incentives whose profits are exempt from taxation. It also helps in better marketing of certain specified goods manufactured and exported out of India, which in turn, stimulate and increase import of capital goods including machinery so essential to the industries.

Tax avoidance helps in the growth of Industries, Total tax exemptions helps institutions to meet their financial obligations also in a better way, tax avoidance is beneficial to capital formation in the country, promotes savings and investments in the country.

Tax avoidance brings in loss to the state Exchequer.

Conclusions and Suggestions

“Every light has its own shadow” is also true in the case of Income Tax of the country, specially in regard to Income Tax Deductions, exemptions etc. The Income tax concessions and exemptions were used to avoid and evade

the tax. Income tax is a direct tax as such, its Burden cannot be shifted, so Income tax payers always tries to evade and avoid Income Tax because they are the only escape with the tax-payers.

We can suggest some suggestions for effective tax revenues to the Government and tax payers also as under:

The waxed problem of evasion and avoidance of Income tax has always drawn the attention of government, Income tax authorities, tax-bar members and tax payers. Consequently, appropriate steps have also been taken from time to time, yet there is no break in the problem. The suggestions given by the different study groups, enquiry committees, investigation commissions, researcher etc., have all been discussed by us in detail at appropriate places, while dealing with different aspects of the foregoing pages of this study.

Some important suggestions are given as below:

1. Simplification and Rationalisation of Indian Income Tax Act.
2. Uniform Application of Law throughout the Country
3. Determination of Jurisdiction
4. Early Finalisation of Proceedings
5. Reduction of tiers of appeals
6. Encouragement of savings
7. Measures to plug loopholes and removal of Anomalies
8. Establishment of a National Income Tax Commission
9. Incentives to the honest tax-payers

In the last we would like to consider that the problem of evasion and avoidance of tax can be removed only when the rationalisation and simplification of taxation laws is done without any loss of time. The co-operation of the tax-payers in the shape of voluntary compliance is also of unique importance. We hold the view that the problem of evasion and avoidance of tax deserves co-operation and contribution of every class of society including leaders, tax-payers, officials, economists, social reformers and the nationalists.

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