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## Can Modi Tackle The Black Money Beast?

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Indians have been hiding money from their rulers for centuries. The best way to secrete your wealth away was to turn it into gold, and either wear it or bury it. Little wonder that India was the world's biggest gold buyer last year. It consumed 842.7 tonnes of gold, despite the Indian economy not doing too well in 2014, gold jewellery sales rose 8% to an all-time high of 662 tonnes.

Prime Minister Narendra Modi said. He noted that even the creation of new black money would be in peril with steps announced by Jaitley against benami or no-name, shell transactions. Jaitley said he would table a new law to chase illegal money parked abroad. Under the new law, evasion of tax in relation to foreign assets will be slapped with a jail term of 10 years, a penalty rate of 300%, and no appeal; false tax returns hiding foreign assets will fetch seven years in prison; and banks and institutions abetting evasion will also be punished. A Benami Transaction Prohibition Bill would also be enacted, to curb domestic black money. Any purchase or sale over Rs 100,000, or \$1,600, would be tagged by a taxpayer's identity number.

Three days after top HSBC executives apologised to British lawmakers for control and compliance failures that allowed the bank's Swiss tax scandal, called Swiss Leaks, India's government swore its implacable enmity for black money and illegal funds flows.

"People with black wealth are no longer safe. Other than prison, they have no other future," Prime Minister Narendra Modi said. He noted that even the creation of new black money would be in peril with steps announced by Jaitley against benami or no-name, shell transactions.

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India's black money problem goes back a long, long time. Government after government has sworn that it will drive a stake through the heart of this dark demon, and been thwarted by India's complex tax laws, corrupt officials, and deep-pocketed tax evaders. The two or 3% of Indians who actually pay income-tax - mostly salary-earners who have no choice - continue to pay more real tax than the richest 2 to 3%. Jaitley said he would tack a 2% surcharge on 'super-rich' Indians who earned more than Rs 10 million (\$161,000) per year. Guess what? There are only about 100,000 people who have declared that income or more. This in a country of 1.25 billion which has the world's third-largest number of dollar billionaires - 97 in all.

In 1956 when the brilliant Cambridge economist Nicholas Kaldor was persuaded by P.C. Mahalanobis, the father of Indian statistics and the architect of the country's second five-year plan, to examine the young nation's tax structure. Kaldor estimated India's black economy was between Rs 2 and 3 billion - a massive figure then, but ten times what the government itself estimated.

How does that stack up against the situation today?

A December 2014 report from the Washington, DC-based Global Financial Integrity estimates that developing and emerging countries lost \$6.6 trillion in illicit financial flows from 2003 to 2012. It said these illicit flows grew at a rate of 9.4% annually, more than twice the rate of global GDP growth.

In the GFI study, India moved up from fifth to fourth place between 2013 and 2014 among the top ten developing economies with the maximum illicit fund leakages, behind China, Russia and Mexico. During the decade ending 2012, GFI estimated India alone had lost \$439.59 billion. In 2014 alone, the loss totalled about \$95 billion.

According to a tax expert, if \$440 billion represents illegal money stashed abroad by Indians, an equal, if not greater, sum is circulating in subterranean India. Together, that's just a little shy of a trillion dollars.

Let's put that in context. India's economy is estimated to be about \$1.5 trillion. The total size of India's central budget for 2015/16 is 17.77 trillion rupees, or \$287 billion.

Are Modi and Jaitley likely to succeed where others have failed? For the first time, the government is moving beyond penalties to arming income-tax authorities with the power to prosecute defaulters. But visibly uneasy business leaders quizzed on television after Jaitley's budget speech warned that India could slide back into nasty tax policing and harassment, where political scores could be settled and corruption would again erupt in a tax compliance structure that had begun to smell clean at last.

The Modi government is not the first to threaten tax evaders with imprisonment. Two years ago, the Congress-led UPA government also prescribed jail time of up to seven years for failure to pay service tax. Evasion of customs and excise duties have also been a criminal offence.

**"The two or 3% of Indians who actually pay income-tax - mostly salary-earners who have no choice - continue to pay more real tax than the richest 2 to 3%."**

In 2011, when the Congress government said it planned to imprison income tax evaders, Modi's own Bharatiya Janata Party, then in opposition, spoke out loudly against such a 'draconian' step. Yashwant Sinha, who was the BJP finance minister in 1998 when the dreaded Foreign Exchange Regulation Act (FERA) was repealed and replaced with the more liberal Foreign Exchange Management Act (FEMA), said the Congress government was over-reacting to calls

to curb black money. "Any law that the government is drafting has to be carefully thought through and clear distinction should be made between minor evasion and major evasion of ill-gotten wealth. There should be very careful consideration of all facts before any law is drafted," he told the Times of India. The government quietly dropped that idea.

The Modi government has been trumpeting its success in persuading Swiss authorities to part with information. In fact, the HSBC data was leaked in early 2008 by French-Italian whistleblower Herve Falciani. He gave French authorities data on more than 100,000 HSBC account-holders from more than 200 countries. The Indian Express, part of a global consortium of investigative newspapers given access to the



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data, reported on February 9 that 1,195 Indians - many business tycoons and some politicians - held accounts in HSBC's Swiss private banking arm as of 2006-07. More than 400 of those accounts are either legitimate or held no money. The newspaper said Indian tax authorities have so far brought in more than \$500 million of undisclosed income.

In fact, the credit for the first - and so far most successful - breakthrough in identifying and prosecuting illegal Swiss bank account holders goes to the U.S. Internal Revenue Service. That success led, in March 2010, to the Foreign Account Tax Compliance Act, or FATCA, which compels foreign governments and banks to report bank accounts, or foreign entities in which U.S. taxpayers hold a stake.

Critics say the cost of implementing FATCA, both for the United States and the governments and foreign institutions it deals with, outstrips the taxes and penalties that the IRS has recovered.

But there is no doubt that FATCA has fathered a growing global consensus on attacking the offshoring of illegal wealth. Group of 20, or G20 ministers and central bankers agreed in April 2013 on automatic exchange of information on offshore tax evasion.

Indian tax evaders fall into three categories:

1. corrupt politicians, bureaucrats and government employees;
2. old-economy big business houses;
3. and mid-sized businesses, traders and exporters-importers.

The second and third categories perfected their dishonesty in the days when India's tax rates were punitive: in 1973-74 the highest individual tax rate rose to a whopping 97.5%. Tax avoidance and evasion became inevitable, and flourished.

India's new-economy entrepreneurs are largely honest taxpayers. In the end, better tax compliance stems from clear rules, proper implementation, and reasonable tax rates. With a rising proportion of transactions taking place online, tax authorities have mountains of data, but do not use it efficiently. The Modi government has emphasised technology as a means to curb corruption. Why then is it harking back to the bad old tax days?

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