

Voluntary disclosure of income scheme analysis



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HISTORY OF ECONOMIC THEORY PAPER

PHILOSOPHISING A LAW: VOLUNTARY TAX DISCLOSURE

- Joanna Thomas

A. THE LAW

The Voluntary Disclosure of Income Scheme was launched by on the 18th of June, 1997. It continues for six months until the 31st of December, 1997. It was launched by The Central Board of Direct Taxes. Its aim was to unearth disclosed income, to provide income tax and wealth tax defaulters an opportunity to disclose their income at the prevailing tax rates, while under the umbrella protection of immunity from all major laws relating to economic offences, and to mobilise resources and channel funds into priority sector of the economy.

Those opting for the VDIS would be granted immunity from prosecution under the Foreign Exchange Regulation Act, 1973, the Income Tax Act, 1961, the Wealth Tax Act, 1957, and the Companies Act, 1956. ¹

In the six months of its existence, 4, 75, 477 people disclosed their assets and incomes under VDIS. This garnered a revenue of 33, 697. 32 crore rupees to the Indian Finance Ministry on which Rs. 9, 729. 02 crore were paid as tax.

While some saw the scheme as a success that boosted the government's coffers, others were outraged. A Public Interest Litigation (PIL) was filed in the Supreme Court under the argument that schemes like VDIS penalised honest tax payers while at the same time, it encouraged tax evaders.

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A. 1. FEATURES

The salient fetters of the scheme include:

1. The declarant would have to file a declaration before the Honourable Commissioner of Income Tax. The Commissioner would then grant him a certificate, setting forth the particulars of the voluntarily disclosed income and the amount of income tax paid in respect of the same. This provided the declarant immunity from prosecution under the Income Tax, 1961. A person may make a declaration in respect of any income chargeable to tax for any assessment year prior to the assessment year 1998-99:

- for which he has not filed a return under section 139 of the Income Tax Act.
- for which he has failed to disclose in a return of income furnished by him under the IT Act before the date of commencement of the Act.
- which has escaped assessment in terms of section 147 as it stood prior to 1. 4. 1989 and thereafter.

2. The scheme covered all persons, both corporate and non-corporate. The tax payable on the disclosed income was 30% for individuals and 35% for all other declarants, i. e., corporates and firms. The tax on the voluntarily disclosed income or wealth would have to be paid before making the declaration, and proof of such payment was to be attached along with the declaration.

3. Those who opted for the VDIS would be granted immunity from prosecution under the Foreign Exchange Regulation Act, 1973, the Income Tax Act, 1961, the Wealth Tax Act, 1957, and the Companies Act, 1956.

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4. A person in whose case a search under section 132 of the Income Tax Act has been initiated or where books of account, other documents or other assets have been requisitioned under section 132A will not be entitled to make a declaration in respect of the previous year in which the search was made or any earlier previous year.

B. THE PHILOSOPHICAL WORKINGS

P. Chidambaram, the mastermind behind the VDIS, claimed that broadening the tax-net through VDIS was a more goal than how much the scheme could net. Of the 4, 66, 031 respondents from VDIS, most were part of the 12 million who formed the tax-net. Most of these 12 million were grossly under-reporting their revenues and with this amnesty they were able to change their black money to white money at a much lower rate. Chidambaram ended up protecting the right of tax evaders. This goes against the philosophy of equitable taxation.

The amnesty scheme hampered the government's regular tax collection as tax-evaders, specially businessmen, non-salaried professionals who could opt out of the tax net, found it cheaper to declare their incomes with the lower tax rates of the amnesty schemes. In addition to that, as this scheme was anticipated in advance, the tax evaders were able to dodge paying taxes — which could be seen by a drop in revenue collections — before the scheme actually arrived. This was what happened with the VDIS. Evaders were aware from March that the tax pardon was on its way and hence, personal income tax collections in the first seven months of the current fiscal year recorded a significant drop. A post-VDIS drop also occurred, as has been seen in the

case of earlier amnesty schemes. Therefore, despite the 'record haul', the government emerges as a net loser in this scheme as the VDIS hampered long-term tax collections that in effect proved the government's crusade against corruption to be a sham. ²

Actually, pardons provided at regular intervals may shrink the tax base instead of expanding it, as Chidambaram expected. It encourages more tax-dodging. Before the 80's pardons were witnessed at the rate of once every twelve years. However in the 1990's, amnesties were witnessed six times in eight years. Hence, Chidambaram's threat that the VDIS would be the last opportunity for evaders to come clean, didn't hold much ground.

Another claim of Chidambaram was that an objective of the VDIS was to mop up black money. But how much can an amnesty work towards absolving an evader? According to a study done by NIPFP in the 1980's, black money in India was valued at 18-21% of the GNP. Other independent assessments, however, estimated the value to actually be around 50%. Even assuming a low rate of 10%, in the 1990's, with GNP at 12.6 million crore rupees, the black money in the country can be estimated to be 1.26 million crore rupees. When you compare this to the amount disclosed through VDIS, it barely accounts for 2.5%. And the VDIS was supposed to account for black money of years past!

It can be said that the VDIS provided just the right loopholes that tax evaders were looking for. It provided immunity from various laws and also gave evaders legitimacy for ownership of single units of property in overseas areas and investments in bonds, debentures, shares, fixed deposits etc.

Further, declarations under VDIS could not be used as evidence against the declarant in those proceedings that involve penalty imposition or litigations under acts such as IT Act, Wealth Tax Act or Companies Act.

Take the example of the son of a very senior Congress leader from Andhra Pradesh who declared Rs. 700 crores under the VDIS. The massive loot was amassed over the years from cuts and kick-backs. By paying Rs. 200 crores he can now pocket the rest of the booty which now becomes white and rest assured that he can safely skirt all legal probes in the future. ²

Declarations were made even minors, 2472 declarations to be exact, whose income were joint with that of their parents. This was permitted by the CBDT clarification which was actually inconsistent with the stated law. A test check revealed that these ‘ minors’ declared undisclosed income on dates prior to their birth!

Loopholes could also be found in the declaration of jewellery or silver articles. Initially, the clarification was to assess bullion and jewellery purchased prior to 1 April 1987 at the rates prevailing as on that date. However, this clause was amended later in November that stated that bullion and jewellery should be assessed at the rates that were prevailing on the date of acquisition or purchase, only if a “ credible” proof of purchase or acquisition could be provided. Unfortunately, “ credible” proof was left unexplained and undefined. This loophole provided the most used channel for money laundering under the scheme. Due to this loophole, tonnes of silver was shown in backdated purchases when prices were much lower than the current prices thus reducing the effective rate of taxation. Another

negative effect was that silverware dealers began providing fake receipts to anyone who needed one. In this way, the VDIS provided a lucrative opportunity to create legalised assets by converting undisclosed assets with a much lower effective tax rate. This could be the reason why land, gold and jewelry declarations was far more than that of cash. But this, however, could also be explained with the fact that black money is generally not kept in cash.

Another failure of the Scheme was to lay down valuation requirement for real estate properties. This gap was taken unfair advantage of by the declarants who were able to declared their assets at insanely high values and also managed to protect themselves with the immunity provisions of the VDIS. A property that was purchased earlier in part with black money and shown in registration records at the value equaling the white money involved, could now be declared at its real price i. e. the black and the white money combined. Today, with an appreciation in the value of the property, the declarant could sell and purchase a bigger property with the newly acquired white money.

C. THE VERDICT

The VDIS was drafted with a number of gaps. This was, in turn, compounded by CBDT circulars, clarifications and press briefings that completely benefitted the declarants, i. e., the tax evaders. A number of gaps was left in procedural matters in the implementation of the Scheme. This impacted revenue realisation. The department was deprived of legitimate revenues due to the undervaluation of jewellery and bullion. In addition to this, the

capital loss that arose from jewellery and bullion declarations contributed to the wiping out of the immediate revenue generated from their disclosures in a few years time.

The department had also not instituted any special mechanism that would monitor the declarants in post-VDIS period.

The government had recently announced an amnesty scheme for service tax offenders. This was the Service Tax Voluntary Compliance Encouragement Scheme. The scheme was in effect till December 2013 and is believed to have fetched around 6000 crore rupees to the government. Finance Minister Chidambaram said the government will not be able to announce any more amnesty schemes for the next 20 years. This was due to various factors which includes curbs imposed by the Supreme Court. “ Such schemes cannot be announced every year. There is a Supreme Court judgement on VDIS which actually ties up our hands in announcing a scheme on the lines of VDIS,” Chidambaram was quoted as saying by the PTI.

In conclusion, there is little doubt about which section of society actually benefits from these kinds of amnesty schemes. For honest tax payers, i. e., mainly the salaried class who pay tax at source at higher rates, this is a direct violation of equal tax for equal income. It also shows the government’s impotence in ensuring compliance by the bourgeoisie to come clean. In the mean time, the ruling class eagerly waits for the next amnesty, as he/she knows fully well that amnesties are means to not only for exonerate oneself from crimes but also provides ample opportunities for one to commit further crimes.