

# INTERNATIONAL JOURNAL OF LEGAL SCIENCE AND INNOVATION

[ISSN 2581-9453]

---

Volume 6 | Issue 3

2024

---

© 2024 *International Journal of Legal Science and Innovation*

Follow this and additional works at: <https://www.ijlsi.com/>

Under the aegis of VidhiAagaz – Inking Your Brain (<https://www.vidhiaagaz.com>)

---

This Article is brought to you for free and open access by the International Journal of Legal Science and Innovation at VidhiAagaz. It has been accepted for inclusion in International Journal of Legal Science and Innovation after due review.

In case of **any suggestion or complaint**, please contact [Gyan@vidhiaagaz.com](mailto:Gyan@vidhiaagaz.com).

---

**To submit your Manuscript** for Publication at **International Journal of Legal Science and Innovation**, kindly email your Manuscript at [editor.ijlsi@gmail.com](mailto:editor.ijlsi@gmail.com).

---

# Tax Avoidance vs. Tax Evasion: A Critical Examination of Legal Boundaries in Indian Taxation Law

---

SHASHI BHUSHAN<sup>1</sup>

## ABSTRACT

*This dissertation explores the differences between tax avoidance and tax evasion in Indian tax law. It investigates how these practices affect government revenue and fairness. Through analysing laws, real cases, and regulations, it finds challenges in distinguishing legal tax planning from illegal evasion. The study suggests ways to make the rules clearer and enforcement stronger for a fairer tax system in India.*

**Keywords:** Tax Avoidance, Tax Evasion, Legal Boundaries, Indian Taxation Framework, Penalties.

## I. INTRODUCTION

Taxes play a crucial role in funding public services and programs in any society. However, there's a fine line between legal tax planning and unlawful tax evasion. In India, understanding this difference is essential for ensuring fair taxation and government revenue.

This paper explores the distinction between tax avoidance (using legal strategies to lower taxes) and tax evasion (illegally avoiding taxes) in India's tax laws. By looking at laws, real cases, and regulations, it aims to clarify the rules and strengthen enforcement for a fairer tax system.

## II. UNDERSTANDING TA

### (A) Definition & Conceptual Framework:

TA can be called an art not to pay taxes without infringing any tax law and not reducing a tax burden. Avoiding taxes is simulated a chain of transactions in consequence of which a tax payer gets tax benefit.<sup>2</sup>

The term "TA" indicates the use of legal strategies to reduce their tax commitments. Individuals and companies can use this technique. It includes planning finances in a strategic manoeuvre and taking advantage of the tax law benefits or loopholes. It's a litigation approach that reduces

---

<sup>1</sup> Author is a student at Amity Law University, Noida, India.

<sup>2</sup> Definition of TA, its Features and Relationship with TE, Definition of TA, its Features and Relationship with TE, <https://ojs.mruni.eu/ojs/public-policy-and-administration/article/view/2368>

your tax responsibilities by using legal practices. Compared to unlawful TE, it does not purposefully misrepresent transactions or income.<sup>3</sup>

Scholars emphasize that TA is a legitimate way of reducing tax liabilities through legal means within the boundaries of the law, distinguishing it from illegal TE, which involves fraudulent techniques like falsifying deductions or underreporting income.

This practice is built into the tax code to encourage certain behaviours like saving for retirement or buying a home while indirectly subsidizing essential services such as health insurance and higher education.<sup>4</sup>

TA in India is covered under the General Anti-Avoidance Rule (GAAR). It is an anti-TA law under Chapter X-A of the IT Act, 1961. It allows tax officials to deny tax benefits if a deal is found without any commercial purpose other than TA. GAAR was introduced in India by then Finance Minister, Pranab Mukherjee, on 16 March 2012, during the Budget session introduced vide Finance Act, 2012. This legislation aims to prevent TA by targeting arrangements or transactions that are specifically designed to avoid taxes.<sup>5</sup>

### **(B) Strategies & Mechanisms Employed:**

Strategies used by individuals often differ to the one utilised by businesses.

Some TA strategies used by individuals include<sup>6</sup>:

- **Investing in Municipal Bonds:** Municipal bonds offer tax-free interest income, making them a popular choice for individuals looking to reduce their tax liability.
- **Aiming for Long-Term Capital Gains:** Holding assets for the long term can lead to lower tax rates on capital gains, providing a tax-efficient way to grow wealth and reduce tax commitments.
- **Starting a Business:** Launching a side business not only generates additional income but also offers various tax advantages, allowing for deductions on business-related expenses and reducing overall tax liability.
- **Maximizing Retirement Accounts and Employee Benefits:** Contributing the maximum allowable amount to retirement accounts like 401(k)s and taking advantage of employee benefits can help individuals reduce their taxable income and lower their tax burden.

---

<sup>3</sup> TA, <https://www.5paisa.com/stock-market-guide/tax/tax-avoidance>

<sup>4</sup> What Is TA and How Is It Different from TE, [https://www.investopedia.com/terms/t/tax\\_avoidance.asp](https://www.investopedia.com/terms/t/tax_avoidance.asp)

<sup>5</sup> General Anti-Avoidance Rule, Chapter X -A, IT Act, 1961

<sup>6</sup> 6 Strategies to Protect Income from Taxes, <https://www.investopedia.com/articles/personal-finance/032116/top-6-strategies-protect-your-income-taxes.asp>

- Utilizing Health Savings Accounts: Health savings accounts (HSAs) provide a tax-advantaged way to save for medical expenses, with contributions being tax-deductible and withdrawals for qualified medical expenses being tax-free.

These strategies demonstrate how individuals can legally reduce their tax liabilities by leveraging various investment options, business ventures, retirement accounts, and health savings accounts to optimize their tax planning.

Some TA strategies used by businesses include:

- Investing in Tax-Advantaged Schemes: Businesses can reduce their tax liability by investing in tax-advantaged schemes like retirement plans, which offer tax benefits and deductions.
- Utilizing Tax Shelters: Tax shelters provide legal ways for businesses to lower the amount of taxes they have to pay, allowing them to invest in initiatives that offer tax advantages.<sup>7</sup>
- Offshoring: Some businesses move money to offshore tax zones with lower tax rates and financial secrecy laws to reduce their tax burden, taking advantage of loopholes that allow for tax minimization.
- Claiming Deductions and Credits: Businesses can engage in TA by maximizing deductions and credits available to them under the tax laws, reducing their taxable income and overall tax liability.<sup>8</sup>
- Strategic Financial Planning: By structuring finances through legal entities like corporations or trusts, businesses can minimize their tax commitments within the boundaries of the law.

These strategies illustrate how businesses can legally reduce their tax liabilities by leveraging various investment options, tax shelters, offshore accounts, deductions, and credits to optimize their tax planning and financial management.

### **III. EXAMINING TE**

#### **(A) Definition and Key Characteristics:**

TE is the illegal non-payment or under-payment of taxes, usually by deliberately making a false declaration or no declaration to tax authorities – such as by declaring less income, profits or

---

<sup>7</sup> Supra Note 11

<sup>8</sup> Strategies Employed by Multinational Companies to Avoid Tax, <https://www.linkedin.com/pulse/strategies-employed-multinational-companies-avoid-tax-eyitayo/>

gains than the amounts actually earned, or by overstating deductions. It entails criminal or civil legal penalties.<sup>9</sup>

Key characteristics of TE include<sup>10</sup>:

- **Deliberate Non-Compliance:** TE involves a deliberate and intentional act of non-compliance with tax commitments, where individuals or entities purposefully fail to report income, profits, or gains accurately to tax authorities.
- **False Declarations:** TE often entails making false declarations or no declarations to tax authorities, such as declaring less income, profits, or gains than actually earned, or overstating deductions to reduce tax liabilities.
- **Criminal or Civil Penalties:** Engaging in TE can lead to criminal or civil legal penalties, including fines and imprisonment, as it is considered an illegal activity that undermines the tax system and results in revenue loss for governments.
- **Associated with Informal Economy:** TE is commonly associated with the informal economy, where individuals or businesses engage in illegal activities to avoid paying taxes, such as hiding income, using bribes, or manipulating financial information.
- **Contrast with TA:** TE differs from TA, as it involves illegal actions to evade taxes, while TA focuses on legally minimizing tax liabilities through exploiting loopholes or exceptions in tax laws.

### **(B) Illegal Practices and Fraudulent Schemes:**

Illegal practices and fraudulent schemes under TE include:

- **Concealment of Income:** Concealment of income is a common method of TE, where taxpayers intentionally hide their true income from tax authorities to pay lower taxes. This fraudulent practice involves not disclosing actual earnings in tax filings, using cash transactions to avoid a paper trail, or providing false information to underreport income. By concealing income, individuals evade taxes and violate tax laws, leading to potential criminal charges and penalties. This deceptive act undermines the tax system and results in revenue loss for governments, highlighting the seriousness of TE as a criminal offense.<sup>11</sup>
- **Not Filing Income Tax Returns:** Not filing income tax returns is a form of TE where

---

<sup>9</sup> TE, Transparency International, <https://www.transparency.org/en/corruptionary/tax-evasion>

<sup>10</sup> Ibid

<sup>11</sup> TE, <https://scripbox.com/tax/tax-evasion/>

taxpayers intentionally avoid submitting their income details to tax authorities, leading to the concealment of income and evasion of tax liabilities. This practice involves individuals failing to fulfil their legal obligation to report their earnings accurately, thereby hiding income and not paying the taxes owed. By not filing income tax returns, taxpayers engage in illegal activities that undermine the tax system, potentially resulting in criminal charges and penalties.<sup>12</sup>

- **Incorrect Income Tax Returns:** Incorrect income tax returns are a common method of TE where taxpayers intentionally file inaccurate tax returns to evade taxes. This deceptive practice involves individuals understating their total income, presenting false deductions or exemptions, or inflating expenses to pay lower taxes than owed. By filing incorrect income tax returns, taxpayers engage in illegal activities that violate tax laws and lead to revenue loss for governments. This fraudulent behaviour can result in severe penalties, including fines and potential criminal charges, highlighting the serious consequences of TE.<sup>13</sup>
- **Forged Documents:** Incorrect income tax returns are a common method of TE where taxpayers intentionally file inaccurate tax returns to evade taxes. This deceptive practice involves individuals understating their total income, presenting false deductions or exemptions, or inflating expenses to pay lower taxes than owed. By filing incorrect income tax returns, taxpayers engage in illegal activities that violate tax laws and lead to revenue loss for governments. This fraudulent behaviour can result in severe penalties, including fines and potential criminal charges, highlighting the serious consequences of TE.<sup>14</sup>
- **Default in Filing TDS Return and/or TCS Return:** Default in filing Tax Deducted at Source (TDS) return and/or Tax Collected at Source (TCS) return can be considered a form of TE. When individuals or entities fail to submit these returns as required by law, they are not fulfilling their obligations to report the taxes deducted or collected at the source.<sup>15</sup> This non-compliance can lead to underreporting of income, evasion of tax liabilities, and ultimately, a violation of tax laws. By defaulting in filing TDS and TCS returns, taxpayers engage in practices that undermine the tax system, potentially

---

<sup>12</sup> Ibid

<sup>13</sup> TE – Examples, Types, and Insights, <https://www.tookitaki.com/glossary/tax-evasion>

<sup>14</sup> Ibid

<sup>15</sup> TDS And TCS Return Filings, <https://www.ahujaandahuja.in/services/outsourcing-services/tds-tcs-return-filings/>

resulting in penalties and legal consequences.<sup>16</sup>

### **(C) Legal Framework in Indian Taxation**

The legal framework governing taxation in India is established by the Constitution, which allocates legislative powers, including taxation, among the Union Government, State Governments, and Local Bodies. Schedule VII of the Constitution enumerates the subject matters of taxation across three lists, empowering the Union Government, State Governments, and Local Bodies to levy various duties and taxes.

#### **a. Income Tax Act, 1961:**

The Income Tax Act of 1961 serves as a comprehensive legislative framework governing the taxation of income in India. Comprising 23 chapters and 298 sections, the Act aims to achieve multiple objectives, including promoting economic stability, employment generation, and economic development. It applies to income earned from all sources within the previous year, determining tax liabilities based on relevant income tax slabs and allowing certain deductions per financial year. The Act covers both direct and indirect taxes, distinguishing between taxes paid directly by taxpayers based on their income and those levied by the government during goods and services transactions. It provides avenues for appeals to the High Court and Supreme Court, outlines tax assessment procedures, and delineates the roles of tax authorities. Key sections such as 80C, 80CCD, 80CCC, 80TTA, and 80TTB enable taxpayers to claim deductions for various investments, contributions, and expenses. Tax Avoidance (TA) is a legal method of reducing tax liability under the Act, while Tax Evasion (TE) is illegal and punishable. Penalties for TE can range from 100% to 300% of the tax for undisclosed income. The Act also addresses taxation on insurance premiums, with Goods & Services Tax (GST) applicable to such payments. Amendments to the Act are periodically made to reflect evolving fiscal policies.

#### **b. Goods & Services Tax (GST) Act, 2017:**

The Goods & Services Tax (GST) Act of 2017 represents a significant legislative milestone in India, unifying multiple indirect taxes into a single GST framework. This comprehensive tax system operates across various stages of the supply chain, applying to both goods and services transactions. Intra-state transactions are subject to Central GST and State GST, while inter-state sales attract Integrated GST. The Act incorporates provisions for transitional arrangements, input tax credit regulations, and the continuation of pre-existing procedures.

---

<sup>16</sup> Due Dates for E-Filing of TDS & TCS Returns for FY 2023-24, <https://blog.saginofotech.com/due-dates-of-e-filing-of-tds-or-tcs-return>

Transitional measures include input tax credit claims through Form GST TRAN 1, subject to submission within ninety days of the appointed day. The Act addresses input tax credit for previously exempted goods now taxable and tackles tax avoidance and evasion through rigorous measures. It aims to streamline cross-border trade and ensure revenue collection through customs duties.

**c. Customs Act, 1962:**

The Customs Act of 1962 governs the import and export of goods in India, facilitating the levy, assessment, and collection of customs duty. The Act comprises various chapters addressing distinct aspects of customs administration, including definitions and interpretations, powers and responsibilities of officers, classification and valuation of goods, levying and collecting customs duty, clearance procedures, trade facilitation, electronic document filing, seizure and confiscation of goods, appeals and revisions, court jurisdiction and powers, and administration. The Act aims to facilitate seamless cross-border trade while ensuring revenue collection through customs duties. It undergoes periodic amendments to accommodate evolving trade practices and align with international conventions.

**d. Finance Act:**

The Finance Act enacts the financial proposals of the Central Government for a fiscal year. For instance, the Finance Act of 2017 introduced amendments to several laws, including the Income-tax Act of 1961, the Cinematograph Act of 1952, the Electricity Act of 2003, and the Competition Act of 2002. The Act incorporates provisions concerning qualifications, appointment, tenure, remuneration, and other terms of service for various regulatory bodies and tribunals, aiming to ensure effective governance and regulatory oversight. Amendments to the Income-tax Act introduce provisions for regulating the qualifications, appointment, tenure, remuneration, and other terms of service for members of regulatory bodies and tribunals, providing clarity regarding their functioning. The Act also amends the Competition Act to reinforce its provisions and enforcement mechanisms.

**e. Double Taxation Avoidance Agreements (DTAA):**

Double Taxation Avoidance Agreements (DTAA) are treaties signed between two or more countries to eliminate international double taxation and promote trade, investment, and economic cooperation. India has entered into DTAA with numerous countries, aiming to provide relief from double taxation and offer preferential tax rates to taxpayers operating across borders. Under the Income Tax Act of 1961, provisions for avoiding double taxation are outlined, allowing taxpayers to claim relief for taxes paid to countries with which India has



DTAA. DTAA ensures tax certainty and fosters economic exchanges between nations.

**f. Taxation of Securities Transaction Act, 2004 (STT Act):**

The Securities Transaction Tax (STT) Act of 2004 imposes a direct tax on transactions involving the purchase and sale of securities listed on recognized stock exchanges within India. STT replaced the prior system of levying stamp duty on securities transactions, aiming to generate revenue for the government and deter speculative trading. STT rates vary based on the type of security and transaction, with both buyers and sellers liable to pay. The Act aims to ensure tax compliance and contribute to government revenues, impacting investor returns and market liquidity.

#### **IV. LEGAL BOUNDARIES IN TA**

**(A) Statutory Provisions**

The statutory provisions in India related to TA are crucial in regulating the practice of minimizing tax liability within the boundaries of the law. The Indian legal framework addresses TA through various laws and judicial interpretations. Some key statutory provisions and legal principles related to TA in India include:

**(B) General Anti-Avoidance Rules (GAAR):**

GAAR, embedded within the Income Tax Act of 1961, aims to curb Tax Avoidance (TA) and ensure fair taxation across different income brackets. It targets otherwise lawful practices that undermine tax laws' intentions, focusing on arrangements aimed primarily at obtaining tax benefits. GAAR applies to transactions primarily for tax benefits or lacking sound commercial principles. When invoked, the Assessing Officer refers potential GAAR cases to the Tax Commissioner, who issues notices to taxpayers. Taxpayers can contest such notices, but if unsatisfied, the case is referred to the Approving Panel. GAAR faces criticism for implementation challenges and the thin line between permissible and objectionable tax avoidance. Introduced in 2012, GAAR came into effect in 2017 to combat aggressive tax planning and revenue losses.

**(C) Legislative Intent Rule:**

The Legislative Intent Rule ensures tax laws are interpreted according to legislative intent. It guards against misinterpretation, aligning transactions with statutory goals. Consistent with this rule, valid transactions claim associated tax benefits, while those deviating risk being deemed impermissible avoidance arrangements. Courts employ this rule to prevent misuse or abuse of tax laws, ensuring equitable application and deterring noncompliant strategies.

**(D) Machinery Provisions vs. Charging Provisions:**

Tax statutes comprise Charging Provisions, imposing tax liabilities, and Machinery Provisions, outlining tax assessment procedures. Charging provisions demand clear legislative intent, strictly construed, while machinery provisions are liberally interpreted to fulfill statutory objectives. Distinction between these provisions influences tax assessment and collection, ensuring effective enforcement while upholding legislative intent.

**(E) Double Taxation Avoidance Treaties (DTAA):**

DTAAs are bilateral or multilateral treaties between nations aiming to alleviate double taxation and promote economic cooperation. India has signed over 80 DTAAs, offering various benefits such as tax relief, investment facilitation, and transparency. To qualify for DTAA benefits, individuals must meet residency criteria and furnish relevant documentation. DTAAs offer relief through exemption or tax credit methods, fostering fair taxation and cross-border investment.

**V. CASE LAW ANALYSIS**

The case laws and judicial interpretations of TA in India involve a nuanced understanding of legal principles and judicial decisions that shape the landscape of tax law in the country.

**1. *McDowell & Co. Ltd. v. CTO (1985)*:**

This case holds utmost relevance in Indian tax jurisprudence, challenging traditional approaches to TA disputes. The case highlighted the evolution of judicial decision-making methods in resolving TA issues, distinguishing between the 'Interpretational Approach' and the 'Judicial Test Approach'. The Interpretational Approach involves invoking traditional principles of statutory interpretation, while the Judicial Test Approach introduces new rules or tests to address complex tax scenarios<sup>17</sup>.

**2. *Balaji vs Income-Tax Officer (1961)*<sup>18</sup>:**

This case emphasized the importance of preventing TE through legislation aimed at the prevention of TE. The court upheld the validity of laws designed to prevent TE, ensuring that the classification for such laws is rational and related to the objective of preventing TE.

**3. *Vodafone International Holdings BV v. Union of India (2012)*<sup>19</sup>**

---

<sup>17</sup> Paper: TA Jurisprudence in India: Questioning the Avoidance Jurisprudence in India: Questioning the Traditional additional Narrative, The National Law School Business Law Review (NLSBLR), Volume 5 Issue 1, available at: <https://repository.nls.ac.in/cgi/viewcontent.cgi?article=1067&context=nlsblr>

<sup>18</sup> 1962 AIR 123

<sup>19</sup> Civil Appeal No.733 of 2012

In this case, the Supreme Court of India made a significant ruling nullifying a capital gain tax demand of INR 12,000 crore. The ruling clarified the limitations of Indian revenue authorities in taxing offshore transactions involving non-resident entities acquiring controlling interests in Indian companies. This case addressed a clear instance of TA, highlighting the complexities and implications of cross-border transactions on taxation<sup>20</sup>.

These cases and interpretations reflect the evolving nature of TA jurisprudence in India, showcasing the judicial responses to complex tax scenarios, the need for legislative measures to prevent TE, and the challenges in addressing TA in the context of international transactions.

### **(A) Interpretations and Challenges**

TA is a significant challenge in India, with the country's tax legislations containing numerous anti-avoidance rules. The maneuver of framing the GAAR has been ongoing since 2009, with the rules coming into effect from 2017<sup>21</sup>. Despite the existence of these rules, TA continues to pose a threat to the Indian economy.

One of the main reasons for TA is high tax rates, which can create an incentive for individuals and businesses to seek legal and illegal means to reduce their tax liabilities<sup>22</sup>. This can lead to the misuse of tax provisions, such as rebates for tuition fees, medical expenses, and donations, which are then exploited to evade taxes<sup>23</sup>.

The impact of TE on the Indian economy is significant. It can lead to a reduction in economic growth, as TE and the existence of a parallel economy undermine the effectiveness of taxation laws<sup>24</sup>. The govt. loses money as a result of TE, which might increase the gap and force it to create more money or issue more bonds, which would increase prices.

The govt. has proposed measures to combat TE, such as promoting a cashless economy, which can help lower TE and improve tax compliance. In addition, the govt. has put in place GAAR, which attempts to reduce revenue losses that the govt. incurs from intensive TA strategies.

Despite these efforts, implementing anti-TA regulations is challenging due to the difficulty of differentiating between various types of TA practices. The moral debate surrounding TA also complicates the issue, as some argue that there is a moral entitlement to legally avoiding taxes,

---

<sup>20</sup> TE AND TA - IMPACT OF INDIAN ECONOMY, © 2023 IJCRT | Volume 11, Issue 12 December 2023 | ISSN: 2320-2882, available at: <https://ijcrt.org/papers/IJCRT2312064.pdf>

<sup>21</sup> General Anti Avoidance Rules in India: The story so far! *British Tax Review* (2023 Issue 5), pp. 695-703, available at: [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=4704309](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4704309)

<sup>22</sup> *Supra* note 53 at 33

<sup>23</sup> A critical analysis on TE and indian economy, © 2022 IJCRT | Volume 10, Issue 11 November 2022 | ISSN: 2320-2882, available at: <https://ijcrt.org/papers/IJCRT2211014.pdf>

<sup>24</sup> Impact of TE on indian economy, *IJCAR* Volume7, available at: <https://journalijcar.org/issues/impact-tax-evasion-indian-economy>

while others maintain that the standards for judging the morality of TA exist independently of legal standards<sup>25</sup>.

Thus, TA remains a significant challenge in India, with its impact on the economy and the government's efforts to combat it being a complex issue.

## VI. LEGAL BOUNDARIES IN TE

### (A) Legal Consequences and Penalties:

Legal consequences and penalties of TE in India can be severe and encompass both civil and criminal repercussions. Key aspects include:

**Civil Penalties:** Under the IT Act, individuals found to have concealed income or furnished inaccurate particulars of income may face civil penalties. These penalties can be a percentage of the tax sought to be evaded and are specified under Sections 270A, 270AA, and 271 of the IT Act.<sup>26</sup>

- **Underreporting and Misreporting of Income:** Section 270A (1) of the IT Act addresses underreporting and misreporting of income. Individuals who underreport their income may face a penalty equal to 50% of the tax payable on the underreported income. If the underreported income is due to misreporting, the penalty can be as high as 200% of the tax payable on the underreported income.
- **Failure to Keep Records:** Section 271A deals with the failure to maintain proper records. Taxpayers who fail to keep the necessary records as required by law may be subject to penalties under this section.<sup>27</sup>

### (B) Prosecution and Criminal Penalties:

TE can lead to criminal prosecution if tax authorities believe there has been a wilful attempt to evade taxes. Criminal proceedings under Section 276C of the IT Act can result in imprisonment ranging from three months to seven years, along with fines. In serious cases where the amount of tax evaded exceeds a certain threshold, the punishment can be enhanced, leading to higher terms of imprisonment.<sup>28</sup>

---

<sup>25</sup> Supra Note 50 at 33

<sup>26</sup> What is the punishment for TE in India, <https://law4u.in/answer/3214/What-is-the-punishment-for-tax-evasion-in-India>

<sup>27</sup> Penalties and Prosecution, Income Tax, <https://incometaxindia.gov.in/Charts%20%20Tables/Penalties%20and%20Prosecutions.htm>

<sup>28</sup> Supra Note 34

**(C) Asset Attachment:**

Asset attachment is a significant penalty for TE in India, allowing tax authorities to seize and sell the assets of individuals who have evaded taxes to recover outstanding dues. The IT Act, 1961, empowers tax authorities to attach various types of properties, both movable and immovable, including bank deposits, shares, securities, insurance policies, and immovable properties. Before attaching any property, tax authorities must serve a notice to the taxpayer, specifying the amount owed and the reasons for attachment. Once the property is attached, it can be auctioned, and the proceeds are used to settle the tax liabilities. However, if the taxpayer pays the taxes along with penalties and interest, the attached property will be released from attachment. Asset attachment is a crucial tool used by tax authorities to ensure compliance with tax laws and to recover unpaid taxes from individuals who engage in TE.<sup>29</sup>

**(D) Black Money Act:**

The Black Money (Undisclosed Foreign Income and Assets) and Imposition of Tax Act, 2015, provides for stringent penalties and prosecution for undisclosed foreign income and assets.<sup>30</sup>

- **Tax Liability:** The Black Money Act prescribes a flat rate of 30% as tax liability on undisclosed incomes and assets held in foreign countries. Taxpayers with undisclosed foreign income are subject to this tax rate.<sup>31</sup>
- **Penalties:** Individuals found to have undisclosed foreign income or assets can face penalties under the Black Money Act. Section 41 of the Act provides for a penalty equivalent to three times the black money tax. This means that in cases where undisclosed amounts are identified, a total of 120% of the undisclosed amount becomes payable (30% tax plus a penalty equivalent to three times the tax).<sup>32</sup>
- **Criminal Prosecution:** The Black Money Act allows for criminal prosecution in cases of non-disclosure of foreign assets in income tax returns or evasion of black money tax. Section 50 of the Act provides for criminal prosecution for non-disclosure of foreign assets, while Section 51 covers prosecution for evading black money tax. These criminal proceedings can lead to imprisonment

---

<sup>29</sup> Attachment of Property under Income Tax Law, <https://enterslice.com/learning/attachment-of-property-under-income-tax-laws/>

<sup>30</sup> The Black Money (Undisclosed Foreign Income & Assets & Imposition of Tax Act, 2015

<sup>31</sup> Prosecution Under Black Money Act for Inherited Foreign Bank Accounts, <https://www.indialawoffices.com/legal-articles/prosecution-under-black-money-a>

<sup>32</sup> India: An Illustrative Inquiry Under the Black Money Act, <https://www.mondaq.com/india/income-tax/1325670/an-illustrative-inquiry-under-the-black-money-act>

ranging from three years to ten years, along with fines.

### **Other Penalties:**

Failure to file income tax returns on time can result in penalties, with late fees ranging from Rs. 5,000 to Rs. 10,000. Non-compliance with Tax Deducted at Source (TDS) regulations can lead to fines ranging from Rs. 10,000 to Rs. 1,000,000, depending on the violation. Additionally, failure to pay tax as per self-assessment or not complying with TDS regulations can result in penalties up to the total amount of tax owed to the government.<sup>33</sup>

These legal consequences and penalties underscore the seriousness of TE in India, emphasizing the importance of compliance with tax laws to avoid severe financial and legal repercussions.

### **(E) Enforcement Mechanisms**

The GOVT. detects TE through various mechanisms, including investigations by the Central GST (CGST) formations, the use of technology and data analytics, and the implementation of rewards for informants.

### **(F) Investigations by Central GST (CGST) formations**

These investigations formations play a crucial role in detecting and addressing TE in India. These investigations involve a series of actions taken by tax authorities to combat TE effectively. The CGST formations initiate investigations into cases of GST evasion and violations, with a focus on curbing TE and ensuring compliance with tax laws.

As of December 2018, the CGST formations had initiated investigations in 3626 cases of GST evasion/violations in the current financial year. The total amount of tax involved in these cases was estimated to be Rs. 15278.18 crore, with Rs. 9959.29 crore recovered from the total detection amount in the same financial year.

Furthermore, the CGST formations have been proactive in utilizing technology and data analytics to enhance their investigative capabilities. The Directorate General of Analytics & Risk Management (DGARM), established by the Central Board of Indirect Taxes and Customs (CBIC), serves as an apex body for data analytics and risk management. The DGARM leverages internal and external data sources for data mining and analysis, generating targeted outputs for field formations and investigation wings of CBIC. This strategic approach has resulted in the detection of Rs. 677.68 crore and the realization of Rs. 43.06 crore till November

---

<sup>33</sup> What is TE? All You Need to Know About, <https://www.legalkart.com/legal-blog/what-is-tax-evasion-all-you-need-to-know-about>

2018.<sup>34</sup>

Overall, the investigations conducted by CGST formations, coupled with the use of technology and data analytics, are instrumental in detecting instances of TE, ensuring compliance with tax laws, and recovering evaded tax amounts to uphold the integrity of the tax system in India.

### **(G) Use of Technology and Data Analytics**

The GOVT. is leveraging technology and data analytics to detect TE effectively. The Income Tax Department is actively employing AI algorithms to sift through vast datasets, identify patterns, and detect potential instances of TE. The govt. has implemented Project Insight, an initiative that utilizes advanced analytics and artificial intelligence to scrutinize taxpayer data, identify potential risks, detect irregularities, and formulate targeted enforcement strategies.<sup>35</sup>

The GOVT. is also contemplating a heightened use of technology-driven advanced risk profiling to prevent input tax credit (ITC) fraud in the GST Tax (GST) regime. This involves utilizing artificial intelligence (AI) and data analytics to identify ITC frauds and halt suspected claims until undergo thorough scrutiny.

The govt. has detected GST evasion of ₹2,54,235 crore in the last three financial years, with only 27.7% or ₹70,617 crore recovered so far. To tackle fraudulent credit claims, the GOVT. is considering establishing a strong system of risk profiles to serve as an early warning for potential suspects, subjecting these individuals to thorough physical scrutiny before granting registration.<sup>36</sup>

The use of technology has made detection of TE much easier, with the department recovering ₹36,000 crore till December 20, 2020, and expecting the number to go up to at least ₹50,000 crore by the end of the fiscal year. The department uses a mix of generative AI, advanced AI, and machine learning, which is customized for the department and continuously updated every quarter<sup>37</sup>.

Thus, the GOVT. is utilizing technology and data analytics to detect TE effectively. The Income Tax Department is employing AI algorithms to scrutinize taxpayer data, identify

---

<sup>34</sup> Detection of GST Evasion, Press Information Bureau, GOVT., available at: <https://pib.gov.in/Pressreleaseshare.aspx?PRID=1559126>

<sup>35</sup> ABP News Article, Digital Overhaul: How India's Tax System Is Revolutionising With Technology, available at: <https://news.abplive.com/business/india-s-tax-system-is-revolutionising-with-technology-digital-overhaul-tax-automation-1674934>

<sup>36</sup> SAG InfoTech Blogs, Govt Consider AI and Data Analytics to Combat GST Evasion, available at: <https://blog.saginfotech.com/govt-consider-ai-data-analytics-combat-gst-evasion#>

<sup>37</sup> The Economic Times, Tech helps I-T department recover Rs 36,000 crore, available at: <https://economictimes.indiatimes.com/news/india/tech-helps-i-t-department-recover-rs-36000-crore/articleshow/106330092.cms>

patterns, and detect potential instances of TE. The GOVT.is also contemplating a heightened use of technology-driven advanced risk profiling to prevent input tax credit (ITC) fraud in the GST regime. These measures aim to enhance the efficiency of tax collection, strengthen the government's ability to detect irregularities, and promote a fair and effective tax administration in India.

### **(H) Rewards for Informants**

The GOVT. has implemented various reward schemes to incentivize informants who provide specific information about TE, benami transactions, and undisclosed black money.

#### **1. Income Tax Informants Reward Scheme:**

- Informants can earn rewards for disclosing information about benami transactions, properties, and undisclosed black money held abroad.
- Under the Benami Transactions Informants Reward Scheme 2018, informants can receive rewards up to Rs 1 crore for providing specific details actionable under the Income-tax Act, 1961<sup>38</sup>.
- Informants sharing information about undisclosed black money held overseas under the Black Money Act can earn rewards up to Rs 5 crore<sup>39</sup>.

#### **2. Central GST (CGST) Reward Schemes:**

- The govt. offers rewards to informers and govt. employees for disclosing and reclaiming assets and properties connected to unpaid taxes, duties, and fines under various govt. schemes.
- Informants can receive rewards of up to 20% of the net selling earnings of seized illegally transported goods, duties evaded, and fines recovered.

#### **3. Maneuver and Conditions:**

- Informants are eligible for rewards only when the entire dues have been recovered, the case is closed after adjudication, appeals, and prosecution in courts, which may take several years.
- The reward amount is contingent on the recovery of the evaded amount, and informants

---

<sup>38</sup> Business Today, I-T Dept's new scheme: Inform govt about TE, get rewards up to Rs 5 crore, available at: <https://www.businesstoday.in/latest/policy/story/it-dept-new-scheme-inform-govt-about-tax-evasion-get-rewards-up-to-rs-5-crore-149511-2018-06-01>

<sup>39</sup> The Economic Times, Be an informer to income tax department, earn up to Rs 5 crore, available at: <https://economictimes.indiatimes.com/news/economy/policy/be-an-informer-to-i-t-dept-earn-up-to-rs-5-crore/articleshow/64415664.cms>



may receive rewards based on the recovered amount, subject to certain conditions and limitations.<sup>40</sup>

These established reward schemes encourage individuals to report instances of TE, benami transactions, and undisclosed black money. These schemes offer financial incentives to informants who provide specific information leading to the recovery of evaded taxes, with rewards varying based on the nature and extent of the TE detected.

## VII. CASE STUDIES

The following case laws demonstrate the legal boundaries of evasion, with a focus on the interpretation of tax laws, the validity of tax legislation, and the consequences of tax fraud:

### 1. **McDowell & Co. Ltd. v. Commercial Tax Officer**<sup>41</sup>

This case is a significant ruling in Indian tax law that addressed the distinction between TE and TA. In this case, McDowell & Company, a liquor manufacturer, paid sales tax under the Andhra Pradesh General Sales Tax Act, 1957, based on turnover that excluded excise duty. However, the Sales Tax Authorities contested this position, leading to a legal battle that reached the Supreme Court.

The Supreme Court determined that excise duty, as defined in section 2(10) of the A.P. Excise Act, 1968, is applicable to the manufacture of liquor, and the duty must be paid before the liquor can be removed from the distillery. Buyers of Indian liquor from McDowell's distillery obtained distillery passes for liquor release after payment. McDowell's accounting records did not reflect excise duty paid by purchasers. Consequently, McDowell paid sales tax under the Andhra Pradesh General Sales Tax Act, 1957, based on turnover excluding excise duty.

The court revisited its earlier decision in McDowell's case [1977] 1 SCR 914 and concluded that excise duty is directly linked to manufacturing and constitutes part of turnover under the Sales Tax Act. It emphasized that tax planning within legal bounds cannot constitute TA. Additionally, the court reiterated that a colourable device within legal confines cannot be considered part of tax planning. Moreover, the court clarified that the Supreme Court cannot entertain pleas not raised in the High Court.

Subsequent rulings have analysed the McDowell case concerning double TA agreements (DTAAs). The court emphasized that if the DTAA intended to exclude nationals of third states, it should have explicitly stated so. Furthermore, the court asserted that the judiciary is

---

<sup>40</sup> SAG InfoTech Blog, Simplify All Govt GST Reward Schemes for Fraud Informants, available at: <https://blog.saginfotech.com/gst-reward-schemes>

<sup>41</sup> 1985 AIR 1653

responsible for assessing such transactions' legitimacy. It referred to the US-India Double TA Convention, which expressly prohibits third-state nationals from benefiting from the agreement. The court noted that such transactions were envisaged by the legislature, and the India-Mauritius DTAA's failure to address them explicitly suggests legislative acceptance of non-residents exploiting the agreement to their advantage.

## **2. MakeMyTrip (India) Pvt Ltd vs Union of India<sup>42</sup>**

The MakeMyTrip (India) Pvt. Ltd. case of TE involved the Directorate General of Central Excise Intelligence (DGCEI) alleging that the company had evaded service tax by not depositing the tax collected from customers for hotel bookings. The DGCEI had initiated coercive measures, including the arrest of the Vice President (Finance) of MakeMyTrip, Mr. M.K. Pallai, on 8th January 2016, and searches of the premises of other online travel providers. The Company challenged the DGCEI's actions, claiming that they had been cooperating with the investigation and that the DGCEI was aware of their activities and service tax position since 2006. The company also argued that there was no need for the arrest of Mr. Pallai, as they were cooperating with the investigation and providing the required information.

The ruling by the court was as follows:

- **Suspicion of TE:** The judgment mentions that arrests were made by the Directorate General of Central Excise Intelligence (DGCEI) based on suspicions of TE or failure to deposit service tax collected. However, the court emphasized that such arrests should not be made without following due maneuver and without proper determination of liability.
- **Procedure for TE Cases:** The court outlined the procedural requirements for addressing cases of TE. It stressed the need for issuing show-cause notices, conducting inquiries, and adhering to the provisions of the Finance Act, 1994 (FA) before taking coercive measures like arrests.
- **Misuse of Arrest Powers:** The judgment criticizes the DGCEI for acting hastily and recklessly without following the prescribed procedure, suggesting that such actions were based on suspicions rather than concrete evidence of TE.
- **Refund of Alleged Dues:** The court directed the DGCEI to refund the amounts deposited by the petitioners towards alleged service tax dues, implying that the

---

<sup>42</sup> W.P.(C) 525/2016 & CM 2153/2016

payments were made under the assumption of tax liability due to alleged TE.

Relevance: It addresses the procedural aspects and safeguards to be followed when dealing with cases involving suspected TE.

## **VIII. CONCLUSION**

In conclusion, this paper has shed light on the complexities surrounding tax avoidance and tax evasion within the Indian taxation system. By examining legal boundaries, case studies, and enforcement mechanisms, we've highlighted the challenges in distinguishing between lawful tax planning and illegal evasion. Moving forward, it's imperative to address these challenges, clarify the rules, and strengthen enforcement to ensure a fair and equitable tax system in India.

\*\*\*\*\*