ISSUES RELATED TO BLACK MONEY

Pooja Rangaprasad

Black money or Illicit money has been defined by Ministry of Finance in their report 'White Paper on Black Money' as assets or resources that have neither been reported to the public authorities at the time of their generation nor disclosed at any point of time during their possession. This would include money earned from crime (such as drug trafficking, smuggling, arms trafficking, sexual exploitation and prostitution etc), corruption and commercial tax evasion (such as underreporting revenues and inflating expenses). Although the focus of the black money debate in the country has been mainly on corrupt money, according to a report on black money by the Central Board of Direct Taxes, Measures to Tackle Black Money in India and Abroad, the main method for generation of black money in India is through commercial tax evasion by underreporting revenues and inflating expenses adopted by a range of business entities.

While estimating the scale of illicit or black economy in the country is difficult, some attempts have been made to measure this globally. According to Global Financial Integrity (GFI), a Washington DC based organisation, from 2002 to 2011, developing countries lost US$ 5.9 trillion to illicit outflows. China leads the list with a loss of US$ 1.08 trillion from 2002 to 2011. India was the fifth largest country with cumulative outflows worth US$ 343.9 billion from 2002 to 2011, which they claim is a conservative estimate. These estimates do not include the movement of illegal money through the *hawala* system, smuggling and cross-border cash transactions; all of which are significant in the Indian context. GFI estimates that for every $1 that poor nations receive in foreign aid, $10 in illicit money flows offshore. This movement of money out of developing countries, including India, is facilitated by a network of over 60 tax havens which enables setting up of *benami* trusts or corporations ensuring that the real owners of the business remain unknown. According to Tax Justice Network, an international coalition of researchers, the global super-rich have at least $21 trillion hidden in secret tax havens at the end of 2012. In 2011, Government of India had commissioned three national-level institutes, National Institute of Public Finance and Policy (NIPFP), National Institute of Financial Management (NIFM) and National Council of Applied Economic Research (NCAER), to assess and provide estimates of the extent of black money in India. Once the reports are published, there might be additional clarity on the scale of this problem in the country. While the methodology and data from different studies can certainly be debated for their accuracy, there is no denying the magnitude and importance of addressing the issue. It is especially significant in developing countries where there is a substantial need to expand public revenues to meet the growing needs for developmental expenditure.

Adding to the complexity of this outflow of unaccounted money is that this wealth is not simply lying in foreign bank accounts to be recovered or brought back to the country. In reality, a large portion of this money comes back into India by a process known as 'round tripping' i.e. the money that left the country and ended up in a tax haven is invested back into the country as 'white' money. But there is no data or analysis on how much of the black money is round tripped and comes back into the country. The Union Ministry of Finance's 'White Paper on Black Money' while noting that the two highest sources of FDI into India between 2000 and 2011 were Mauritius (41.80 percent) and Singapore (9.17 percent), stated that "*Mauritius and Singapore with their small economies cannot be the sources of such huge investments and it is apparent that the investments are routed through these jurisdictions for avoidance of taxes and/or for concealing the identities from the revenue authorities of the ultimate investors, many of whom could actually be Indian residents, who have invested in their own companies, through a process known as round tripping*". This makes the issue of 'recovering' black money extremely difficult and it would be much more prudent to invest in mechanisms that will help restrict the outflow of money.

In addition to being low or nil tax jurisdictions, tax havens offer strong secrecy with respect to hiding wealth making them attractive locations for confidentially routing money through them. Individuals and corporations who want to hide their wealth secretly, set up a layer of *benami* trusts or entities using this network of tax havens and loopholes in domestic laws, making it difficult for authorities to know the ultimate beneficial owner i.e who actually owns a business or corporation. Addressing this effectively requires not just fixing domestic loopholes but effective international coordination as well.

Reforms are needed in sectors like real estate, jewellery market and financial markets, which have been identified as some of the sectors most vulnerable to generation of black money. Examples of such reforms include tightening regulations in the financial sector, improved reporting and monitoring mechanisms in the jewellery sector and introducing/improving state legislation to effectively address loopholes in real estate transactions. In addition, measures bringing greater transparency in the global financial system are also needed to act as deterrents to moving money offshore. The introduction of registries (which could be explored making public with adequate safeguards) of beneficial owners of trusts and corporations would have a deterrent effect for those looking to secretly hide their wealth behind *benami* accounts. Effective exchange of information between countries where individuals and corporations hold an account is another important way to increase transparency. India has been very supportive on forums like G20 in pushing for more effective information exchange standards. Stronger reporting standards by multi-national corporations ensuring that they are required to report their sales, taxes paid, profits, employment etc for every country where they are operating will help understand which corporations are misusing these routes by reporting profits in tax havens, where they do not have economic activity, in order to avoid paying taxes.

While the strong public mobilization and pressure on the issue of black money has helped to keep the issue on the political agenda, greater focus is needed on ensuring that money does not leave the country rather than on bringing this money back. Strong political will is required to address this issue not just domestically, but considering the scale of the issue across the developing world, India's responsibility also extends to its actions on international platforms such as the UN, G20 and BRICS.

[The author works with Centre for Budget and Governance Accountability (CBGA), New Delhi (www.cbgaindia.org); she can be contacted at *rpooja@cbgaindia.org*]