

# Black Money Law - an Analysis

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Black Money Law (BML) is a strong action, part of a strong multilateral attack on tax evasion as well as tax planning. In this paper, I am discussing:

Scheme of BML	...	...	Part I
Some unique features of BML and some short comings of BML.	...	...	Part II
A tabular summary of relevant provisions for Computation of Tax Base.	...	...	Part III
BML & Place of effective Management			Part IV

While advising on BML one has to consider FEMA also.

Why I call this series of actions as "Multilateral Attack" is explained.

} Separate  
Articles on  
the subjects.

## Short Forms used in this article:

<b>AO</b>	:	Assessing Officer.
<b>BM</b>	:	Black Money.
<b>BML</b>	:	The Black Money Law: (Undisclosed Foreign Income & Assets) and Imposition of Tax Act, 2015.
<b>Benami</b>	:	Benami Transactions (Prohibition) Act.
<b>Black Income:</b>		Undisclosed Foreign Income.
<b>Black Assets :</b>		Undisclosed Foreign Assets.
<b>CIT</b>	:	Commissioner of Income-tax.
<b>CGT</b>	:	Capital Gains Tax.
<b>COR</b>	:	Country of Residence.
<b>COS</b>	:	Country of Source.
<b>DTA</b>	:	Double Tax Avoidance Agreement.
<b>FATCA</b>	:	U.S. Law asking financial intermediaries to report.

<b>FEMA</b>	:	Foreign Exchange Management Act.
<b>FERA</b>	:	Foreign Exchange Regulation Act.
<b>FIU</b>	:	Financial Intelligence Units.
<b>G20</b>	:	Group of Twenty Nations.
<b>GAAR</b>	:	General Anti-Avoidance Rules.
<b>GOI</b>	:	Government of India.
<b>IR</b>	:	Indian Resident & Ordinary Resident.
<b>IT</b>	:	Income-tax.
<b>ITA</b>	:	Income-tax Act.
<b>LTCGT</b>	:	Long Term Capital Gains Tax.
<b>NR</b>	:	Non-Resident of India.
<b>NOR</b>	:	Not Ordinarily Resident.
<b>PE</b>	:	Permanent Establishment.
<b>PMLA</b>	:	Prevention of Money Laundering Act.
<b>POEM</b>	:	Place of Effective Management.
<b>ROR</b>	:	Resident & Ordinary Resident.
<b>SPV</b>	:	Special Purpose Vehicle.
<b>SAAR</b>	:	Specific Anti Avoidance Rules.
<b>STCGT</b>	:	Short Term Capital Gains Tax.
<b>TDS</b>	:	Income-tax Deducted at Source.
<b>TP</b>	:	Transfer Pricing.
<b>VDS</b>	:	Voluntary Disclosure Scheme. (1997)
<b>VCS</b>	:	Voluntary Compliance Scheme. (2015)

### **History:**

Series of scams by high level politicians were exposed during last fifteen years. People of India were watching with frustration that Government had no desire to act against scamsters. Then came out the list of Indian people holding black money in tax haven banks. Again Government was not acting. Advocate Mr. Ram Jethmalani appealed to the Supreme Court asking for action against Indians holding black money abroad. It was apparent that even Supreme Court was frustrated. Government was simply not acting. In these circumstances Mr. Narendra Modi made an election promise to bring back foreign black money. In May 2014, he won the elections with a significant majority. As a fulfillment of his election promise, Black Money Law has been passed. (Note: this is not a political observation. Events have a direct impact on Tax Laws.)

## I. **Basic Scheme of BML:**

1. Current package of **laws** to attack black money has following parts:

- (i) Enforcement for bringing back black money (under FEMA);
- (ii) Compliance scheme (under BML); and
- (iii) Penalty, prosecution & administration (under BML).

The enforcement provision is permanent. Compliance scheme is temporary. Investigation machinery will be as existing at present under Income-tax Act.

## 2. **Key Sections:**

Section 2 (11) & 2 (12) define “undisclosed foreign asset” and “undisclosed foreign income and asset”.

Section 3 is the charging section and also provides rate of tax.

Section 4 lays down the scope of Tax Base.

Section 5 provides for computation of Tax Base.

Section 10 provides for assessment procedure.

Section 41 provides for penalty.

Section 42 – Penalty for Incorrect Return.

Chapter V – Sections 48 to 58 provide for prosecution.

Chapter VI – Sections 59 to 72 provide for Voluntary Compliance Scheme, charge of tax & penalty under VCS.

As far as jurisdiction for tax, penalty and prosecution are concerned, Black Money Law (BML) and Income-tax Act (ITA) **both operate simultaneously**. Black Income or Asset may be taxable under one or the other; or both laws. However, once an income/ asset is taxed under any one law; it cannot again be taxed under the other law. Double taxation within India is not envisaged. BML is targeted only against “Foreign” black money. ITA covers foreign as well as domestic black money.

## 3. **Important Components of the Scheme:**

### 3.1 **Assessee: Section 2 (2).**

**3.1.1 Residence:** This law (Section 3) applies only to: **Residents** and Ordinary Residents (**ROR**) of India. In other words, if a non-resident has black money abroad, this law does not apply to him. Apparently, the objective of the law is to bring back into India, the black money held abroad by Indian residents.

This legal position arises out of the definition of an assessee. BML makes a new definition of “assessee” which is different from the definition of assessee under the Income-tax Act. Only when a person is liable to pay tax under this law, he is an assessee. Since a non-resident or an NOR is not an assessee under this law, the BML does not apply to him.

However, this law is unique. The applicability may be divided into two parts: (i) Regular charging and Enforcement provisions and (ii) Voluntary Compliance provisions.

- (i) For Regular provisions, Sections 1 to 5 lay down basic provisions. U/s. 2 (2) a Non-Resident is not an assessee. Hence he can't be forced or penalised under BML.
- (ii) However, chapter VI Sections 59 to 72 are voluntary. People are offered an opportunity to come forward and voluntarily comply with the law of the land. S. 59 offers the opportunity to declare undisclosed income and wealth – to ANY PERSON. Hence even if a Non-Resident wants to voluntarily file the declaration; he can do so.

Consider a situation where a person was an Indian resident. He had foreign income which was un-disclosed. Then he became a non-resident of India. **Two possible interpretations:** (i) The black money law will not apply to the person because he is no longer an assessee under this law. (ii) Contrary interpretation: Once a person has not paid taxes in India, that money becomes undisclosed income. Thereafter, even if the person becomes a non-resident of India, the law continues apply to him. In my view, the first interpretation is a better interpretation. This law does not apply to Non-Residents & NORs. Such a person is NOT even an assessee.

**3.1.2 Liable to Tax:** Under Section 2, assessee has been defined. A person becomes assessee if both of the following conditions are satisfy:

- (i) He is resident and ordinary resident (ROR); &
- (ii) He has income or assets liable to tax under BML.

If any one of the two conditions is not satisfied, that person is not an assessee. Residence is discussed in Para 3.1.1 above. Liability to tax is discussed below. For example, there is a person resident and ordinarily resident. He has no black money. He is not an assessee under BML. No action can be taken against him under BML.

**Illustration:** An assessee was resident in the year 2016-17. He earned foreign sourced black money. He was liable to tax under BML. However, his black money was not discovered. In the year 2017-18, he goes out of India and becomes a non-resident. Then he ceases to be an assessee. Now, can the department take action against the person?

One View: The person was liable to tax under BML. **By leaving India, he cannot escape tax.** Action can be taken against him under BML.

Another View: When a person is not even an assessee, how can the Government take action under BML? This will be a controversy. But it is agreed that action can be taken under ITA & FEMA. Only BML does not apply. The reason is – different definitions of “assessee “ under BML & ITA. Suppose that after five years the person returns to India. He becomes resident and ordinary resident. In this situation again Government can take action under BML.

### 3.1.3 Difference between S.3 & S.60:

Under **Section 3** the charge of tax is on an assessee. Hence the two conditions of being ROR and having black money have to be satisfied. Under **Section 60**, “any person” who makes the declaration becomes liable to tax. Hence under Sections 59 and 60, it is not necessary that the person should be an assessee. Hence it is further not necessary that he should be ROR. In other words, even a non-resident can file declaration under Section 59.

Consider a case where a non-resident had black money chargeable to tax in India. He does not file voluntary declaration. In such a case, the charge of tax is under Section 3 and not under Section 60. Hence the controversy of whether a non-resident is liable to tax or not will continue.

### 3.2 Income:

As far as incomes are concerned, BML applies only to **foreign sourced incomes** which are liable to Indian tax but which have not been disclosed in the Indian tax returns.

**Section 2 (12)** defines undisclosed foreign income and asset. Consider a case where an assessee had foreign undisclosed income of \$ 500 every year for 5 years totaling to \$ 2,500. This income became the undisclosed asset of \$ 2,500 in the sixth year. Since both – undisclosed income and undisclosed asset are taxable does the assessee become liable to pay tax on \$ 5,000 or \$ 2,500?

**Section 5 (1) (ii) (b)** provides that income assessed to tax under BML shall not be again considered as undisclosed income. In other words, once an income or asset is assessed to tax under BML, it cannot be taxed again. Hence the assessee will pay tax on only \$ 2,500.

**Section 2 (11)** defines undisclosed Foreign Assets.

**Section 2 (12)** creates a new phrase: “Undisclosed Foreign Income & Asset”. Specifically, this law covers only **assets located outside India**. Indian undisclosed assets are not covered.

The undisclosed foreign income is further specifically restricted to income **earned from a foreign source**. There is no reason why the income is restricted to foreign income. Is there an intention – not to cover undisclosed Indian sourced income? We don't know. But the clear language of the law states that.

However, Indian Sourced Income – if it is held outside India; it is covered by S.2 (11) as undisclosed foreign asset.

### 3.3 Assets:

As far as the asset is concerned; to be covered under BML, only conditions to be satisfied are:

The asset should be undisclosed;

The asset should be located outside India;

And the assessee should be unable to offer satisfactory explanation for the source of the asset.

The asset may be created out of Indian sourced income or foreign sourced income. The Country of Source of Income is irrelevant.

If the assessee has a satisfactory explanation for the undisclosed foreign asset; such asset gets out of the Tax Base. By the term “**satisfactory**” we understand:

If the source of the asset was taxable in India, full tax was paid. If it was not taxable, proper explanation & evidence for the source should be provided by the assessee.

Undisclosed foreign assets form part of the tax base and are treated at par with undisclosed income. Even Indian sourced income if held abroad, becomes undisclosed foreign asset. Hence it becomes a tax base.

**3.4 Consider an illustration.** Mr. I, a doctor is a surgeon in India. In the year 2010, he operated on a foreign patient in India. Hence his income is Indian sourced income. The NR patient directly deposits Rs. 10 lakhs to the credit of the doctor in a Swiss bank. In the year 2014, Dr. went abroad and spent away entire amount.

- (i) Black Money Law (BML) does **not apply to Indian sourced income**. Hence the doctor's professional fees are not covered by this law.
- (ii) BML covers **only assets in existence** on or after 1<sup>st</sup> July, 2015. Since the doctor has already spent the money, there is no asset outside India. Hence BML cannot be applied.

- (iii) In case, doctor **becomes a NR of India**, he will have a third protection. The law cannot be applied to him.

This interpretation is supported by combined reading of Sections 2 to 5 & also is in keeping with the objective of the law. **Objective** is to bring back the black money held abroad. If there is no money, the objective cannot be served. (Note: ITA and FEMA provisions continue to apply to undisclosed incomes.)

### 3.5 Previous Year:

This law makes a unique provision. The **previous year** in which the AO **discovers** the undisclosed income or asset becomes the relevant previous year in which the AO shall charge income-tax. The year in which the income was earned is irrelevant.

Consider the illustration that the income belonged to the year 2010. It was an undisclosed income. AO discovers the income. There is no provision making a presumption that the **income** of the year 2010 will be treated as income of the previous year 2015-16.

BML takes effect from 1<sup>st</sup> July, 2015. If the income pertains to the year 2010-11, it is not covered under BML. Since BML is a permanent law, one can say that it will cover the future generation of black money. As far as income is concerned, **it does not cover income prior to 1<sup>st</sup> July, 2015**. However, if the undisclosed income continues to remain abroad as an asset in some form, it will become a tax base as an undisclosed asset and will be liable to tax under BML.

- 3.6 **Tax:** Section 3, the charging section also provides for rate of tax at 30% of the tax base. Section 60 is an independent charging section for assets disclosed under VCS. This Act has two separate charging sections.

- 3.7 **Assessment:** Section 10 of BML provides for the assessment procedure. Sections 142 to 148 of the ITA have been compressed into one section - 10.

### 3.8 Penalty:

- (i) If a person makes voluntary declaration as per the scheme, under Section 61, he will be liable to pay 30% of the value of Undisclosed Asset as penalty.
- (ii) If the black money is discovered by the Income-tax department, section 41 provides for penalty at three times the amount of tax computed under Section 10. (90% of black money.)

- 3.9 **Prosecution:** Not discussed in this paper.

- 3.10 **Voluntary Compliance Scheme:** Discussed only briefly in this paper.

### 3.11 Inward Remittance:

The BML does not make a provision that the applicant must bring foreign assets back into India. The 60% amount which he has to pay can be paid from Indian funds and then 100% money can be kept abroad. Hence BML by itself does not cause return of foreign money into India. However, FEMA provisions still apply to the person. The protection under Section 67 of FEMA is for the past. Having made disclosure, Section 8 of FEMA will apply and the party must bring back his funds into India. Otherwise, there will be a new violation of FEMA and BML protection will not be available. Ideally, the person concerned should bring back foreign assets into India and pay the 60% tax and penalty.

### 3.12 Observations:

BML is a set of provisions to deal with black money. It covers several provisions from charging section, computation (partial), assessments, appeals & prosecutions. All this in thirty pages. This raises questions:

- (i) Why make a whole separate law? All the powers necessary to tax black money already exist in the ITA. It includes powers to deal with black money abroad. Sections 68 to 69D and S.147 already provide these powers.

In any case, this law does not provide for survey & investigations. For those functions, ITA & existing department have to be used. Even for BML assessments etc., it will be the existing department that will function. Then why a separate law?

- (ii) It should be noted that - BML deals with Black Money. Whether an amount is Black Money or not will be determined by ITA. Income computation is also under ITA.
- (iii) This law creates new phrases and makes deeming provisions. This opens up huge amount of litigation.

## 4. Tax Base:

### 4.1 Tax Base: Scope: Section 4:

Section 4 provides for the Scope of the tax base - "undisclosed foreign income & undisclosed foreign assets" - on which tax can be levied. **We call it Tax Base.**

This is a Unique law. Normally we have Income-tax Act to charge tax on income; and Wealth-tax Act to charge tax on wealth. Under the Income-tax Act, undisclosed assets are taxed u/s. 69 - "Unexplained Investments". Hence the unexplained investment is "deemed to be income" and then taxed. Under BML, no such deeming provision is made.

Asset remains asset. A tax is charged u/s. 3. What is this tax? Section 3 just calls it a "Tax".

Under the ITA, Section 4 charges Income-tax. Under WTA, Section 3 calls it wealth-tax. Under BML it is just a tax. When we discuss Income-tax Act, we refer to taxable income. While discussing Wealth-tax Act, we refer to taxable wealth. Under BML income & assets – both are clubbed together. If we want to give a common noun that covers both income & asset, appropriate term is: "**Tax Base**".

**4.2 Illustration: Facts:** Mr. A had tax paid, white income. He kept a portion of the money abroad. Hence asset was undisclosed.

**Query:** Can it be taxed under BML?

**Opinion:** Scope of Tax Base is given u/s. 4 (1) (c). Undisclosed foreign asset is a tax base. However, such asset is defined u/s. 2 (11). Since full tax has been paid, the source has been explained. Hence while the asset is undisclosed, it does not form part of the Tax Base. Section 4 (1) (a) makes it clear that only that amount is to be considered under BML – which has not been disclosed as income under ITA. And S.5 (1) (ii) (a) gives specific deduction for such amounts. There will be **No Double taxation** of the same income.

**Observation:** Where the source of asset can be explained, the asset falls outside the Tax Base. Hence technically, the assessee cannot file his return under BML – even if he wanted to file. Hence he can't get the S. 67 relief. under BML. The Enforcement Director can proceed against him under FEMA.

It may be noted that the Voluntary Compliance Scheme applies only when there is a tax evasion. There is no VCS for FEMA violations which are not tax violations.

**4.3 Computation:**

- (i) **Section 3 (1)** – Proviso gives a method of computation of the value of undisclosed asset. The value has to be taken as the **market value** on the first day of the previous year. There is no deeming provision making past incomes as income of the previous year 2015-16 or subsequent years. This means that BML does not cover past concealed incomes.
- (ii) **Section 5:** No deduction of any expenses or carry forward losses is available.
- (iii) **Deduction Available: Section 5 (1) (ii) (a): Income assessable under ITA:**

If the assessee can produce evidence that – the whole or any part of his undisclosed asset held abroad – has been assessed to income-tax in India; or is assessable to tax in India; that portion will be reduced from the total value taxable under BML.

**Issues:** It is fair that if an income is taxed under ITA, it cannot again be taxed under BML. However, if the assessee is holding undisclosed asset outside India; it would be a FEMA violation. Hence under amended FEMA, the enforcement officer can go ahead and acquire the assessee's Indian assets. Please see discussion under Part for FEMA.

- (iv) **Section 5 (1) (ii) (b):** Once an amount is considered as taxable under BML; the same amount cannot again be considered as taxable under BML. This has been illustrated above in Paragraph 3.2.
- (v) **Section 4 (2):** Adjustments or additions made during assessment proceedings shall not be considered black money under BML.
- (vi) **Section 4 (3):** Once an income or asset is included as Black Money under BML, the same cannot be considered as income under ITA.

## 5. Applicability of BML:

### 5.1 BML & ITA both continue to **simultaneously apply**.

**1<sup>st</sup> Illustration:** Mr. X had concealed income of the past years. Accumulated income has been kept abroad as concealed asset. If the AO finds out either the asset or the income, he can proceed under BML or under ITA. Issue: who has the discretion to apply BML or ITA? AO or Assessee? As long as the assessee can revise his past returns (upto previous year 2013-14), he has the option. For undisclosed incomes of earlier periods, assessee does not have any option. AO may proceed under that law which is more beneficial to the department.

**2<sup>nd</sup> Illustration:** Mr. IR's NRI uncle gifted him \$ 10,000. U/s. 8 of FEMA, he has to bring the amount into India. Keeping the same abroad is a FEMA violation. There is no tax violation. However, in the next succeeding income-tax return, the foreign asset has to be disclosed. Assume that he has not disclosed the gift. If the AO finds out and enquires; he should be able to give satisfactory explanation. Then it will be a case of incorrect return. Penalty u/s. 42 of BML will be Rs. 10,00,000. However, the asset is not a Tax Base under BML and will not attract tax @ 30% & penalty @ 90%.

### 5.2 The law applies only to **Undisclosed Income and Undisclosed asset**. Consider Section 3 (1) & the proviso. **Once an asset is disclosed**, it is not Tax Base under BML. Once an income has been disclosed, this law cannot apply to it. There may be any amount of disputes during assessment proceedings. Assessee may claim exemption. AO may refuse

the exemption. However, the income or the asset has been disclosed. Hence this law cannot apply.

Simple disclosure of foreign asset in the Indian income-tax return will not be sufficient. Because the income-tax returns being filed will be scrutinised under the existing Income-tax Act. Once a person discloses an asset, he has to explain the source of the income. Otherwise (i) under Section 68 & 69 of the ITA, the AO can add that asset to his income; and (ii) under BML the same can be taxed.

**5.3** BML is not applicable to **Indian sourced incomes**. Let us say \$ 500 Bn. Black Money is lying outside in India. As per an estimate, \$ 450 Bn. is Indian Sourced Income. This won't be covered under the definition of Undisclosed Income. In fact, the applicant cannot even disclose Indian sourced income under the Voluntary Compliance Scheme. Once the money is lying outside India, he can disclose the assets as Undisclosed Assets held abroad.

**5.4** BML is applicable **with effect of 1<sup>st</sup> July, 2015**, for previous year 2015-16 and onwards. There is no specific provision applying the law with retrospective effect. It is not applicable for earlier years. Under ITA, upto 31<sup>st</sup> March, 2016, a person can disclose his past undisclosed income for the previous two years. Previous years 2014-15 & 2013-14, if the assessment is not completed. If the income pertains to earlier years, the same cannot be disclosed under the Income-tax Act. If any assets still survive, the same can be disclosed under BML.

Some Rules & FAQs attempt to cover undisclosed income & assets earned / acquired before 1<sup>st</sup> July, 2015; and not in existence on 1<sup>st</sup> July, 2015. They are ultra vires the Law (BML) and hence invalid to that extent.

**Conclusion:** This law applies to foreign undisclosed assets which exist on or after 1<sup>st</sup> April, 2015; and foreign incomes which are earned and concealed after 1<sup>st</sup> April, 2015.

**5.5 Section 2 (11):**

Undisclosed asset located outside India means an asset (including **financial interest** in any entity).....Which assets are covered and which are not covered? Consider several illustrations of undisclosed assets.

(i)	Mr. IR has Black Money in cash \$ 10,000 lying outside India.	Covered
(ii)	Mr. IR has movable or immovable property situated outside India.	Covered
(iii)	An NRI holds \$ 10,000 benami, for the benefit of IR.	

	This is also, in substance & reality an asset owned by the IR. It may be difficult to find out and difficult to prove. But the asset is covered under BML.	Covered
(iv)	IR is a beneficiary in a Specific Trust settled outside India. The trust has assets in &/ or outside India. IR's beneficial interest is a "Financial Interest".	Covered
(v)	IR is a beneficiary in a discretionary trust. All beneficiaries are Indian residents. The trust itself is taxable as an Indian resident assessee.	Covered
(vi)	IR is a beneficiary in a discretionary trust. One or more beneficiaries are non-residents. The trustees have not allotted any funds to IR.	Not Covered
(vii)	IR has floated a company/ trust in a tax haven. IR is the 100% shareholder/ 100% beneficiary.  All the funds of the entity are invested in India.  The shareholding/ trust benefit is a foreign asset.	Covered

## 6. What the Black Money Law does NOT cover:

### Brief List:

- 6.1 All assets and incomes within India.
- 6.2 All Non-Residents and Not Ordinary Residents.
- 6.3 Incomes arising from Indian Sources.
- 6.4 Gold Monetisation Scheme is not VDS.
- 6.5 There is NO Voluntary Disclosure Scheme (VDS).
- 6.6 S.115 BBD is not a VDS.
- 6.7 BML does not give good and adequate immunity.
- 6.8 In my view, beneficiaries of discretionary trusts are not covered. This is discussed further in a separate article.

## 6. Voluntary Compliance Scheme (VCS): Section 67:

- 6.1 BML under Section 67 provides for protection from proceedings for penalty & prosecution under Income-tax Act, Wealth-tax Act, FEMA,

Companies Act & Customs Act. Hence, wherever there are chances of a person getting caught under any of the laws, one may consider voluntary disclosure; pay 60% & get the protection. **Under Income-tax Act**, if concealed income is found out; tax, interest and penalty together can be far more than 100%. For the same offence, under FEMA, substantial penalty can be charged. Similarly, for the same offence, there can be penalty under different laws. Compared to all these financial costs and a probability of prosecution under several laws, the cost of paying 60% under the compliance scheme may be better.

However, before taking a decision, several issues need to be considered.

## 6.2 NO Immunity - S.67:

It should be clearly noted that there is **NO immunity** granted under the VCS of BML. Section 67 merely provides that: (In simple, separate phrases):

- (i) The **declaration** made by the assessee.
- (ii) Will not be admissible as evidence against the declarant.
- (iii) For penalty; or
- (iv) For prosecution under ITA, WTA, FEMA, Companies Act & Customs Law.

This means:

If the Government gets any other independent information then the Government can use that information to penalize or prosecute the person.

So, if a person is afraid that the Government may/ will get information in any manner:

- (i) under the Information Exchange Agreement or
- (ii) under intelligence by FIU; or
- (iii) by any other person reporting (disgruntled business associate or competitor etc.);

Then he will not get any peace by making this declaration. His 60% money will be lost; and he will still be exposed to all the dangers including  
 - Black Money Law - 120% cost + prosecution;  
 - FEMA - confiscation, penalty & prosecution.

Please note that there is NO protection even against prosecution under BML. (If the department gets independent information.)

Government must give complete immunity under these laws for the scheme to be successful.

- 6.3 The protection is **only for the declarant**. Thus, if one partner in a **partnership firm** makes declaration, other partners and the partnership firm itself will be exposed to all the consequences. One may consider properly before making declaration.

Consider: An Indian Resident **company** has black money abroad. The foreign bank account is held in the name of a director. He has operated the account and used part of the funds. Now the company makes a declaration under VCS and pays 60% of the bank balance existing on 1<sup>st</sup> July, 2015.

Holding assets abroad is a FEMA violation committed by the company and the director. Company gets protection under VCS but the **director** does not get. For getting the protection, director cannot again pay 60%.

7. **Cases where Government has information: Compounding:**

Section 71(d)(iii) provides that Chapter VI shall not apply – i.e. VCS will not be available to any undisclosed asset where information is received by the Competent Authority **under an agreement** (DTA) signed under section 90 or 90A of the ITA. This was generally being understood as if – VCS will not be available in all cases where the Competent Authority has received information – whether under the Agreement or otherwise. In two cases, tax haven banks' lists have been leaked and information has reached GOI. Action has been initiated against many assesseees based on such information received outside the DTA.

On 12<sup>th</sup> August, 2015 newspapers have carried following report: Special Investigation Team (SIT) appointed by the Supreme Court has been investigating Black money held abroad. The SIT has permitted GOI to compound cases of undisclosed assets held outside India even where GOI already has information. Hopefully, necessary circular / notification will be issued by the Government. This will be a great relief for people already under investigation. This compounding will be under the existing provisions of Income-tax Act & not under BML.

**Part I – Scheme of Black Money Law completed.**

## II. Key Issues of the Law:

1. There is a Multi-Lateral attack on tax evasion as well as on tax planning. Consider this law as part of a **macro strategy**. Interpretation and action based on single law can be risky.

2. Consider the impact of FEMA in brief:

Section 13 (1A) and S.37A provide that if the Enforcement Director (ED) **suspects** that a foreign asset is held in violation of FEMA, ED can go ahead and **seize an Indian asset** of equivalent value. He need not give any notice, need not given any opportunity to clarity. Just go ahead and seize the asset. This is a **draconian provision** unfit in any civilised democracy.

For more details, separate article on “Multilateral Attack on Black Money”.

3. BML does not ask to **bring back foreign assets**. That compulsion is under FEMA. Please see Part V.

4. Look at the new legal structure as a **work-in-progress**. This is not the end of the attack on Black Money. In November, 2015, **BEPS** proposals will be published by OECD. These will be further anti-avoidance measures. GOI as member of G20 has committed to make these into Indian tax law.

### 5 Compare with Voluntary Disclosure Schemes:

5.1 Earlier Voluntary Disclosure Schemes permitted massive tax planning. In drafting this law, care has been taken to remove loopholes. One important provision is Tax & penalty have to be paid on current market value. This removes one important loophole.

5.2 In the past, VDS specified tax rates were lower than normal tax rates. A person declaring under VDS was not to pay any penalty and was given good immunities. Finance Minister and CBDT chairman etc. would literally market the VDS. Under BML, the tax and penalty are almost double the normal rate. There is no marketing. There is inadequate relief u/s. 67 and no immunity. Approach is: Government is telling the BM holder - **“Pay up, or else ...”**. None of the past Government was so serious in collecting tax on black money and forcing residents in bringing back their black money.

### 6. Interpretation Games:

Just as children have a weakness for toys and chocolates, we tax consultants have a weakness. The moment, a new law is passed, or a provision is made; our minds start working on (i) preparing schemes to pay tax at a rate much lower than the specified rate; and (ii) interpreting

the law in several manners different from Government intentions. In this VCS, both these weaknesses have to be restrained. Otherwise, the tax payer will be in a serious difficulty. This is not an ethical statement. Practical reasons for this statement are explained in paragraph 8.3 below.

7. For the first time, **intermediaries** like financial institutions and tax consultants have become a serious target under the law - Section 53 of BML, and the action under G20 /OECD plans.

**Issue:** Some **Tax Haven Governments** actively abet tax evasion and tax avoidance. Can they be proceeded against? No. They cannot be proceeded against under ITA or BML. However, as a global action under the G20 plans, tax havens have already started sharing information on tax avoidance. This fact has exposed many people who have avoided tax in the past through tax havens. For such persons, the VCS is the only way out.

## 8. Time Periods for Interpretation:

- 8.1 The law, its application and interpretations may be considered separately for the following periods:

- |       |                             |   |  |
|-------|-----------------------------|---|--|
| (i)   | Pre BML                     | = | Period before 1 <sup>st</sup> July, 2015.  |
| (ii)  | Voluntary Compliance Period | = | 1 <sup>st</sup> July, 2015 to 30 <sup>th</sup> Sept., 2015 or such date to which the scheme may be extended. |
| (iii) | Post BML                    | = | Period after 30 <sup>th</sup> June, 2015.  |

Normally, the interpretation of law cannot be changed based on period. However, there are some weaknesses in drafting. If the law is to be applied uniformly, some provisions may have to be struck down. If some meaning is to be given to the provisions, such division becomes necessary. There is also a very practical reason for different interpretations.

- 8.2 **Pre-BML:** Undisclosed Income pertaining to period prior to 1<sup>st</sup> July, 2015 is not taxable under BML. (See Para I.3.4 and Para II.11.)

- 8.3 **VCS:** When Mr. IR files his declaration under the Voluntary Compliance Scheme - he claims DTA relief under Article 23 of the DTA. Then the Principal CIT will not give certificate in Form 7. Hence even the limited relief under Section 67 will not be available. He will be liable to penal and prosecution proceedings under BML as well as FEMA. The consequences are so harsh that it is not practical for anyone to make a controversial claim under the VCS. In plain language, **VCS is an offer. Take it as offered, or leave it. There is no scope for argument or litigation.**

**8.4 Post BML:** Consider the case where the assessee has not made a particular declaration under VCS. The AO finds information and institutes proceedings under BML. If the AO succeeds, the assessee will end up with following:

Under BML, **120%** tax & penalty + Prosecution.

Under FEMA S.13 (1A) upto **300%** penalty + Acquisition of Indian property - **100%** + Prosecution.

Under FEMA S. 37A acquisition of equivalent value of Indian asset. Hence further loss of **100%**.

**Total loss of upto 620% and prosecution under two laws.**

Altogether the consequences are of the Talibanic proportions. Hence the assessee will certainly fight tooth and nail. He will raise all possible arguments to defend himself.

One of the important arguments may be - the amended provisions under FEMA are unconstitutional. GOI cannot seize assets of anyone without due process of law. In other words, an asset cannot be seized without the Enforcement Director serving a notice and giving a reasonable opportunity to the assessee for explaining his case.

**Hence interpretations of BML will be different under VCS and under BML.**

## **9. Combined Application:**

**9.1** One act of keeping BM outside India may become offense under several laws: (i) Income-tax Act, (ii) BML and (iii) FEMA. If an Indian assessee has black money outside India, it is a violation of all these three laws.

Now even if he makes a Voluntary Compliance Declaration & pays up tax + penalty; he does NOT get any immunity. Only partial relief is given under Section 67.

The section does not specify the time upto which a continuing offense may get relief. For example, the assessee had a residential house abroad as black money. This FEMA violation will not be penalised under FEMA because of VC under BML. But for how long? Once the declaration has been filed, can the assessee continue to hold the assets abroad? Or should he sell the asset and bring the sale proceeds back to India?

How soon he should bring the sale proceeds back? Is it necessary for him to apply to RBI for Compounding/ Regularising the holding of assets? There are **no answers** under the law to all these queries.

- 9.2 **A safe understanding may be:** Sell the assets, bring sale proceeds into India on or before 30<sup>th</sup> September, 2015. In many cases, this may not be practical. For several reasons the sale may take a long time. Then after 30<sup>th</sup> September, 2015, the relief u/s. 67 won't be available.

Best way would be to seek a clarification from the Government. CBDT clarification won't help under FEMA. RBI or Finance Ministry may clarify the matter.

- 9.3 When the assessee sells his assets in the foreign country, it is possible that he will be liable to **Capital Gains Tax** in that country. Some capital gains will be liable to tax in India for the previous year 2015-16 and assessment year 2016-17. The foreign income will be liable to tax in India under normal circumstances under ITA and the foreign tax paid will be available for set off against Indian-tax (if there is a DTA).

Now how does the assessee calculate the **cost of the foreign asset** for calculating capital gains taxable in India? This income will be for assessment year 2016-17 or later. Hence the assessee will disclose the same for the relevant year under ITA. Cost is to be determined u/s. 48 of the ITA. This will be original cost.

**FAQ No. 5** says that the cost will be the **current fair market value** on which tax is paid under BML. There is no such legal provision either under ITA or under BML. Hence we consider this as a relief granted under circular No. 13 of 2015. Once the cost is taken at current market value, the capital gains may be "Nil" or small. Indian tax will be small. Hence claiming credit for the foreign tax paid abroad will not be important. For the Indian assessee, the foreign tax paid will be a "loss".

Assume that Mr. IR pays 20% long term capital gains tax abroad. Balance 80% has to be brought into India under FEMA – Section 8. Out of this, he will pay 60% tax under BML. He will be left with 20% of the current market value of the asset.

10. **Void Declaration & Tax paid:** Assume that the declaration made under Section 59 by the assessee is held by the department to be to be void. BML provides that tax paid shall not be refunded. Is it **constitutionally** valid to accept the money and not to accept the declaration? Lawyers advise that the Government has a **confiscatory right**. If the assessee has made a misrepresentation and hence the declaration has been declared to be void, he cannot seek further relief.
11. **Applicability of BML:** Under BML, there is an **assumption regarding the asset**. The asset becomes taxable in the year in which the AO gets information about the same. However, there is **no such assumption for**

**incomes.** An income remains taxable for the year in which it has been earned.

If income was earned before 1<sup>st</sup> July, 2015 and spent away before 1<sup>st</sup> July, 2015; then BML cannot be applied. Such an income is not taxable under BML.

However, if the income is earned after 1<sup>st</sup> July, 2015 and spent away; and the AO finds out in the year 2025; he can still tax the income for the year in which it was earned. It is not necessary for the AO to tax income in the year in which he got the information. BML has no time barring limit. **Hence black money income (Post BML) will always be liable to tax.**

- 12. "Income" No expenses to be allowed:** An Indian resident assessee is doing foreign business which is not disclosed to Indian authorities. He purchases goods worth Rs. 950 and sells the same for Rs. 1,000. He has made a net profit of Rs. 50. What is the amount taxable under BML?

Black Money law is dependent on the income-tax act. BML does not create a new charge of taxation. When an income taxable under the ITA escapes the tax; then it becomes black money. Thereafter BML applies. BML applies only to the Undisclosed income. There is no applicability to the sales revenue.

It can be said that the goods purchased became assessee's asset. Hence it becomes taxable under BML. However, Section 2 (11) of BML defines Undisclosed assets. **Anything for which the source can be explained is not Undisclosed asset.** In this case, the source for goods worth Rs. 950 is the supplier. Ultimately, only the net profit of Rs. 50 can be taxed.

**Part II - Key Issues of the Law completed**

### III. Computation of Tax Base:

#### Undisclosed Income & Undisclosed Asset for Voluntary Compliance

Sl. No.	Description	Relevant Sections
1.	Exclude all incomes on which Indian tax is paid. BML applies only to Black Money that has escaped Indian tax.	Preamble. Definitions S. 2 (11) & (12) S.3 Specifically S.5 (1) (ii) (a)
2	Black Income & Black Asset - both become Tax Base.	S.2 (12), S.3, S.4, S.72 (c)
3.	While considering Black Income - exclude Indian Sourced Income even if tax is not paid. Note: However, if that income has resulted into a foreign undisclosed asset; then the asset is taxable.	S. 2 (12)
4.	While considering Black Assets - exclude assets situated in India.  Conclusion- One who has no foreign assets/ income need not worry about BML.	S.2 (11) S.60
5.	Foreign assets on which Indian tax was never leviable. Where the source can be explained, the asset is not taxable.	S.2 (11)
6.	Once tax is paid under BML, same income/ asset is not again taxable - under ITA under BML	S.4 (3) S.5 (1) (ii) (b)
7.	Black Income/ Asset which were not in existence on 30 <sup>th</sup> July, 2015.	S.1 (3) as amended by Government order dt. 1 <sup>st</sup> July, 2015. S.O.1790 (E)

This is a quick guide for computation. Some of the steps require detailed explanations/ discussions. Such details are not part of this introductory paper.

**Part III - Computation of Tax Base completed.**

#### IV. BML & POEM:

1. Consider the illustration of a foreign company (SPV) where almost 100% shares are owned by Indian resident. If the POEM is situated in India, the company will be treated as Indian resident. Hence, its **global income** will be taxable in India. If tax is not paid in India, **BML will apply**.
2. Let us further assume that the company is providing certain services. Once it accepts that the Place of Effective Management is situated in India, then the issue will be - whether the services are rendered from India or from abroad. The **service tax** commissioner may examine the place of rendering of services. He may levy service tax on the services rendered by the foreign company.
3. Once the company admits under Indian Income-tax that it has a place of effective management in India; then under the **Company Law**, Section 379 - Chapter XXII may be applicable. Hence the foreign company may be considered as a company doing business in India. Hence it may have to file forms with ROC Delhi.
4. The company may be considered to be a resident of India. However, under **FEMA**, it may continue to be a non-resident of India.
5. Once an Indian resident, it has to do **tax audit**. **TP** may not apply.  
POEM is a vast subject and can take up several chapters - all by itself. In this paper, the attempt is to show a macro attack on tax planning and tax evasion. Suffice it to say that -
  - (i) If Indian residents have formed ten thousand SPVs in tax havens, 9900 SPVs will be treated as Indian residents. Most of these may have to be wound up. Even this may attract substantial taxes.
  - (ii) Tax Haven Governments conduct the business of facilitating SPVs. This business will be in serious jeopardy.

#### Part IV - BML & POEM completed.

This is a part analysis of the Black money Law. In separate chapters I am covering other subjects.

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