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CORPORATE TAX EVASION AND AVOIDANCE: LEGAL CONSEQUENCES

Tax is any charge of money or property that is imposed by a government upon individuals or entities that are within the government's authority to collect. [1]Corporate tax is a direct type of tax levied on the income of a corporate entity which is a separate independent and legal identity, this applies to both domestic and foreign companies. The Union Budget and the Income Tax Act of 1961 apply to these taxes. In the budget announced by Finance Minister Nirmala Sitharaman on February 1st, 2024, she reiterated the measures taken by the government in recent years to reduce and rationalize the tax rates during its tenure, wherein the corporate tax rate was decreased from 30% to 22% (excluding surcharge and cess) for existing domestic companies and to 15% (excluding surcharge and cess) for certain new manufacturing companies.[2] Tax reductions contribute to preventing corporate tax evasion and avoidance. However, the majority of large firms continue to avoid and evade taxes, saving millions of dollars in the process. This results in losses for the government interferes with its ability to carry out its functions, and creates an unfair market.

There is a vanishing line between tax avoidance and tax evasion according to McDowell & Co Ltd. v. CTO, (1985)[3] Judge O Chinnappa Reddy stated in the judgment that, "the shortest definition of tax fraud that I've come across is "the art of dodging tax without breaking the law" Much legal sophistry and judicial exposition have gone into the attempt to differentiate concepts of tax evasion and tax avoidance and the invisible line supposed to exist which distinguishes from the other. Tax avoidance, it seems is legal; tax evasion is illegal."

Tax avoidance is a legal way to reduce the tax burden by taking advantage of loopholes and ambiguities. This is done while complying with the laws. For example, investing in tax-exempt instruments, claiming legitimate deductions, and structuring business for tax efficiency are methods

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[1] Cornell University, https://www.law.cornell.edu/ (last visited, 19 Feb. 24).

[2] Dr. Suresh Surana, Budget '24 makes no structural change in the corporate tax regime, but rate reduction to help, cnbctv18.com,(19th February 2024, 12:48 PM) https://www.cnbctv18.com/business/companies/interim-budget-2024-a-review-in-the-corporate-tax-perspective-18952621.htm.

[3] McDowell & Co. Ltd. v. CTO, (1985) 3 SCC 230.

of avoiding paying taxes. One common instance of tax evasion is the unaccounted cash income that was found hidden away in many Indian households after the demonetization process in November 2016. Many Indian and international firms that have set up shop in India have been exploiting tax havens and subsidiaries to avoid paying taxes since 2005[4]. No penalties or fines are levied as a result of avoiding paying taxes. The government has taken various remedies to curb the problem of tax avoidance like GAAR, Transfer pricing, and POEM.

The Income Tax Act of 1961's General Anti-Avoidance Rule is included in Chapter X-A (GAAR). The Finance Act of 2012 included GAAR in the Income Tax Act, but it wasn't until April 1, 2017, that it became operative. GAAR's sole objective was to stop tax avoidance schemes by using the Income Tax Act's "Section 96[5]. Impermissible avoidance arrangement" clause. Negotiations or arrangements made to obtain a tax benefit were illegal.

After a new corporate residence test was introduced in Section 6(3) of the Finance Act, 2015[6], a foreign business would be considered an Indian tax resident if its place of effective management (POEM) was determined to be in India. Previously, an organization that did not have Indian residency status could only be deemed a resident for tax purposes if its management and control were based there.

Tax evasion, on the other hand, is an illegal and unethical way of not paying taxes. Late filing of income tax returns, non-compliance with TDS regulations, and concealing income are some methods of evading taxes. Chapter XXII of the Income Tax Act, of 1961 states that it is illegal and enlists severe penalties for the same. Tax evading strategies used by huge firms cost several countries, including India, a substantial amount of money. The past twenty years have seen several tax evasion episodes in India. As a result, the government has been forced to amend legislation and treaties with other countries to combat tax evasion. The Indian government put in place several rules and regulations to regulate and stop tax evasion, including the Income Tax Act of 1961 and the Finance Act of 2015. Some provisions of the Income Tax Act 1961 are, Section 270A[7] Penalty for under-reporting and misreporting of income; the penalty is between 100% and 300% of the tax evaded. Section 276C[8] is for a Wilful attempt to evade tax exceeding the amount of 25 lakh

[4] Archismaan Tyagi and Mehu Mohan, Legal Facade of Tax Avoidance in India, Manupatra articles, (19th February 2024, 10:26 PM) https://articles.manupatra.com/article-details/Legal-Facade-of-Tax-Avoidance-in-India.
[5] Income Tax Act 1961, § 96, No.43, Acts of Parliament 1961.
[6] Finance Act 2015, §6(3), No. 20, Acts of Parliament 2015.
[7] Income Tax Act 1961, § 270A, No.43, Acts of Parliament 1961.
[8] Income Tax Act 1961, § 276, No.43, Acts of Parliament 1961.

can invite imprisonment from 6 months to 7 years and a fine. Under section 92E[9] If the taxpayer fails to present a report from an accountant, the penalty imposed is Rs 1,00,000 or more.

Tax planning is the process of decreasing tax liabilities by utilizing different tax provisions. In the landmark judgment of CTO Vs McDowell and Co Ltd in 1985, it was held that "Tax planning may be acceptable provided it is done within the framework of the law." Tax planning strategies are approved by law, and the actions taken are not only allowed but also encouraged by it[10]. To minimize tax liabilities in an annual period, tax planning entails making the best use of tax exemptions, and deductions, and planning for income, expenses, allowances, and refunds.[11]

In conclusion, tax evasion and tax avoidance tactics are not approved by the government and can bring serious consequences. Hence, companies must make use of tax planning to reduce their tax burden.

[9] Income Tax Act 1961, § 92E, No.43, Acts of Parliament 1961.

[10] Archismaan Tyagi and Mehu Mohan, Legal Facade of Tax Avoidance in India, Manupatra articles, (19th February 2024, 10:26 PM), https://articles.manupatra.com/article-details/Legal-Facade-of-Tax-Avoidance-in-India.

[11] Mayashree Acharya, Understanding Tax Evasion and Penalties in India, Clear tax, (20th February 2024, 5:56 PM), https://cleartax.in/s/tax-evasion-and-penalties-in-india