

## **Consequences and Evidence of Tax Evasion and Avoidance**

Meghna Manoj<sup>1</sup>, Meera Gopal<sup>2</sup>

*BCOM Professional, Department of Professional Studies, Christ University, India*  
*Corresponding Author: Meghna Manoj*

---

**ABSTRACT:** *Tax is a major source of government income and it contributes for the general advancement and success of an economy or a nation. The government, in-order to initiate welfare and development programmes which are meant to improve a company's situation, raises revenue in terms of income tax, customs duty, VAT etc. Although, recently it was found that the country had been facing a massive problem with tax evasion. Tax evasion or tax avoidance happens when individuals intentionally fail to pay their tax obligation. This results in revenue loss which may affect the proper functioning of other sectors of the economy. This study explores the tax evasion concepts, covers the reasons and factors responsible and also examines the possible remedies to reduce the problem for the betterment of the economy. For this purpose, the data have been collected from secondary sources.*

**KEYWORDS:** *Government Income, Tax evasion, Tax avoidance, VAT, Revenue*

---

Date of Submission: 04-01-2019

Date of acceptance: 19-01-2019

---

### **I. INTRODUCTION:**

In today's society, taxes are said to be the most important source of financing goods, and it is one of the most powerful tools used for the development of economical and social activities in the economy and in addition, it reduces the imbalance or inequality of salary distribution. There are various types of taxes like income tax, corporate tax, property tax, inheritance tax and they are either classified as direct or indirect tax. Researchers studied the perception of tax professionals with regard to the Indian Income System and they found that the presence of inefficient tax collectors were due to the increase in tax evasion in India. Tax evasion happens when the efforts are made by an individual, a firm's trust and various other entities to avoid paying taxes by illegal and unfair methods. Evasion usually takes place when people intentionally hide their incomes or a part of it from the tax authorities to reduce their tax liability. As a result of evasion, the amount which was to be used for the development of social and economic activities is in turn used for other anti-social activities which are harmful for the economy. Black money and tax avoidance encourage or pave way for control over financial power by undesirable groups in the country. Different kinds of manipulations of financial statements resulting in tax evasions are out of book transactions, parallel books of accounts, manipulation of books of accounts, manipulation of sales/receipts, under reporting of production, manipulation of expenses, and other manipulation of accounts. With relaxation of foreign exchange controls, a lot of new opportunities emerged for tax evasion and because of globalisation, money kept flowing in and out of the country creating tax havens. Therefore, it is of incredible enthusiasm for the government to actualize a financial strategy that fortifies tax compliance. So, as to structure an ideal strategy, it is vital to comprehend the choice procedure of citizens and the fundamental inspirations that impact their conduct. In such manner, the best approach to order and treat the different reactions to tax collection is of crucial significance for scholastic specialists as well as for customary citizens who is installed in social structure and affected by social portrayals.

### **II. REVIEW OF LITERATURE:**

1. (Kang, 2016) In this article "A psychological perspective on tax evasion: Deferential avoidance VS defiant avoidance" Minjo Kang tries to categorise the act of tax avoidance as compliant or non-compliant, it has been brought to our notice that investigation into tax compliance behaviour by various tax payers addresses tax avoidance differently for various reasons thus making it difficult to have a clear understanding of the meaning of tax compliance. Hence the researcher first analysed the meaning of tax compliance and in addition how to understand various behavioural aspects in relation to taxation was of vital importance not only to the academic researchers and the policy makers but also for the ordinary taxpayers as tax behaviour is embedded in the social norms as well as various social representations. The researcher has discussed issues of importance in regard to the conventional conceptualisations of tax avoidance and has also presented a well defined concept of tax avoidance with respect to two factors namely psychological as well as motivational posture.

2. (Alm, 2012) In this paper, “Measuring, explaining, and controlling tax evasion: lessons from theory, experiments, and field studies” by James Alm ,tries to assess the concepts of tax evasion from the information attained since Michael Allingham and Agnar Sandmo launched the modern analysis of tax evasion. He focused on three very specific questions that have emerged over the past few years and arrives at the solutions by highlighting specific examples of his research. The conclusion obtained from this paper highlights the gaps that exist even today in relation to the measurement, explanation and control of tax evasion.
3. (Devarajappa, 2017)- in this article Dr.Devarajappa brings out the major problems faced out in relation to tax evasion cause in the country today. He had pointed out tax to be a major source of government revenue which is meant to be used as a contribution for the overall growth and prosperity of the country. The income of the government is facing a downfall due to the increase in the cases of tax evasion hence leading to bigger economical problems such as black money and so on. The existence of a parallel indian economy brings out the need for major reforms in the indian taxation system in order to address the emerging problems due to tax evasion.
4. (Tarun, Jasmin, Sciences, & Sciences, 2018) In this article “ A study on tax evasion in India” the authors links the act of tax evasion with an informal economy. The total difference between the amount that is suppose to be reported and the amount that is reported is the inequality in the income distribution. The main aim of this paper is to understand the link between tax revenue and tax evasion with the governments revenue. The paper also tries to analyse the main principle of tax avoidance and various loopholes which are used by an individual or an corporate organisation to reduce tax burden. The papers arrives at a conclusion stating that though there is a decrease in the governments revenue , there is still a large number of people who consider paying taxes a burden even though the payable amount is less. The reason for such a psychological constrain might either be due to high tax rates or due to the fact that the tax payers feel that the amount paid by them as that is not used in a justifiable manner by the government.

### **III. RESEARCH DESIGN**

#### **Objectives:**

This study is carried out with the following objectives:

- 1) To understand the various loopholes in the tax system of the country
- 2) To find out the evidence and determinants of tax evasion in the country
- 3) To find out the consequences or impact of tax evasion in the country
- 4) To find out ways to improve the condition or take measures to fight tax evasion

#### **Research Methodology:**

The study done is descriptive in nature, thus describing the current of taxation and the loopholes that exist in the indian tax system which is presented for a span of 10 years. The basis of this study is secondary data which had been obtained from the annual reports published by the Reserve Bank Of India, the press release made by the Finance Ministry and the declarations made by the National Institute Of Public Finance and policy. The study comprises of the data which are provided by the above sources in order to arrive at the various sectors in which loopholes are being exploited to the maximum and contributes to its prevention of it being a part of the major portion of the GDP.

#### **Limitations of the study:**

- This study is completely based on secondary data and the accuracy of the study and analysis is subject to the accuracy of the data
- The period of study only covers till 2017, as RBI does not publish reports on an interim or quarterly basis.
- This study has made a sincere attempt to cover all the areas, but there might be some areas not covered.

#### **Background**

To explain tax evasion, traditional theory has been used and within this theoretical framework, tax evasion has been explained as a function of the probability of detection. (Spicer, 1974). Researchers from various fields such as social psychology, economics, accounting law, tax laws and political science have examined the tax evasion by means of data as well as observation. And based on the results they gathered, ,it was found that although economics effects are important factors or elements, they alone do not appear to be adequate to fully explain and predict the situation. Studies suggested that for a more complete model of tax evasion behaviour, non economic factors should be included as well. For example, age, income earned and moral beliefs have said to affect or influence individual’s natural tendency to engage in tax evasion.

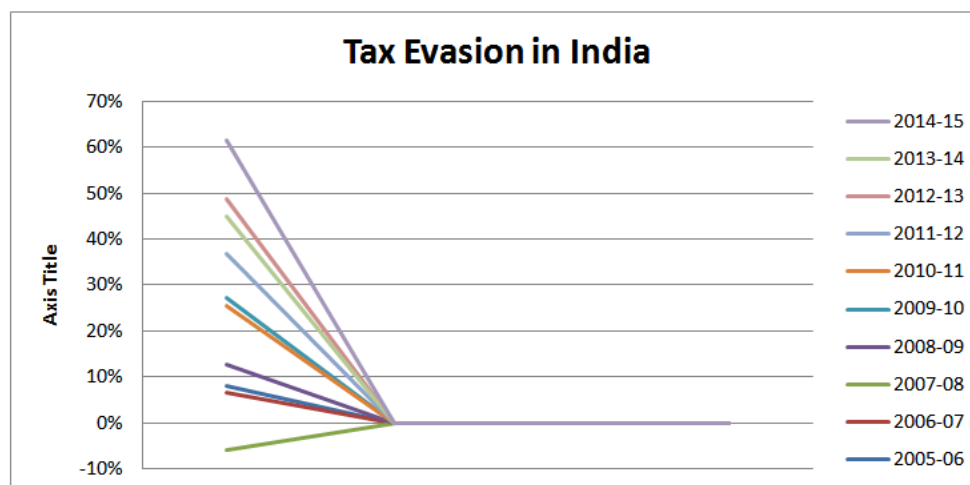
The difference between the revenue estimated and the actual revenue collected is called as the tax gap or the estimated tax evasion. However, tax gap includes the total leakage comprising of tax avoidance, evasion

and corruption. Estimating tax evasion can be done through both direct and indirect methods and these methods over the years have helped understand the amount of tax evasion in the economy.

**Table 1** Shows The Tax Evasion For The Past 10 Years (2005-2016)  
(in crores)

YEAR	REVENUE ESTIMATED	ACTUAL REVENUE COLLECTED	ESTIMATED TAX EVASION
2005-06	170077	165216	4861
2006-07	229272	230181	-909
2007-08	304760	312213	-7453
2008-09	345000	333818	11182
2009-10	387008	378063	8945
2010-11	446000	446935	-935
2011-12	500651	493947	6704
2012-13	565835	558658	7177
2013-14	636318	638543	-2225
2014-15	705628	695797	9831

Sources: (Ministry of finance, 2016)



Source: (Refer Table 1)( in percentage)

### Sources and causes of tax evasion

Mainly tax evasion has three main sources

- 1) Exorbitant rates of taxes
- 2) Lack of transparency/simplicity in tax laws
- 3) Corrupt government administration

In India, corporate try and evade or avoid paying taxes in order to keep some black money to be utilised for exchanges with government bodies and hirelings. Experts avoid paying taxes to save the money for the future as tax rates are very high. Politicians and other law makers for the most part dodge charges since their salary is mainly out of fixes and illicit methods. Tax avoidance is the result of individual citizen behaviour and social standards on the supply side, and inadequacies in tax administration on the interest or demand side. To start with, tax structure needs to see as fair and equal over different gatherings of citizens. Likewise, if marginal rates are very high, people are going to find ways to evade taxes. Over the world, these viewpoints are all around perceived today, and the result of international tax harmonisation has been in lowering in the rate structure (to improve inducements), and attempts at widening the tax base (to lessen disparities).

### Effects of Tax Evasion

Tax evasion has numerous ill effects on the payer, society and total revenue.

- 1) It's most unfavourable influence maybe on equity. A blue collar assembly line labourer pays tax. A restaurant worker whose salary is the equivalent yet who gets some portion of his salary in tips does not uncover it during payment of tax. Along these lines, one worker gains to the detriment of other. This is horizontal disparity or inequity. A salaried employee in a company earns the same, as their incomes appear to be equivalent for tax purposes.
- 2) The tax evasion misshapes economic efficiency. In sectors, that are less subject to the director's investigation, there will be more investment. That may be one motivation behind why certain administration

sector-activities for example, construction companies have developed so sensationally as organization move crosswise over national boundaries in a globalised world economy. Similarly the unorganised sector might try and avoid taxes much more easily than the organised sector. Small tax payers have stayed extremely hard to assess and keep up a steady presence in regulatory corners.

- 3) The functional capacity, efficiency and effectiveness of a sector suffer because of tax evasion as inequity and inefficiency can lead to lower government revenue. Capacity endures because of lower accessibility of assets. The outcome could in all likelihood be an increase in tax rates, or the burden of distortive charges, in this manner starting an endless loop of inequity and disparities.
- 4) Tax evasion being under revealing of pay suggests underestimation of GDP and all its proportionate large scale economic ramifications. Since the denominator is under-evaluated, the proportion of assessment to GDP, the financial deficiency to GDP, and open obligation to GDP are all over evaluated. The perceived higher GDP proportion prompts false solace, yet overstated deflationary action might be made to rein back an overstated financial shortfall or public debt ratio.
- 5) Tax evasion has had a reducing effect on the economy's growth.
- 6) Reduction in revenue and increase in inflation are the direct effects of tax evasion.
- 7) There has been transferring of funds or black money between India and other foreign countries through secret channels, affecting the country's reputation all around the world.
- 8) There would be disequilibrium in the country as the rich get richer and the poor becomes poorer.
- 9) Due to tax evasion by the rich society of the economy, government is forced to increase tax rates to increase the outcome of revenue every year.
- 10) Leads to poor standards of living for the BPL as government doesn't have enough revenue to take welfare measures.

#### **IV. ANALYSIS**

Some of the measures that can be taken to fight tax evasion are:

##### **1) Reducing tax rates**

Predominance of high tax rates is the first and foremost purpose of tax evasion, because this is the thing that makes evasion so profitable or beneficial furthermore, notwithstanding the risks. The present high rates of tax collection leave the government with little extension for mobility for bringing extra assets in the midst of the crisis. The maximum marginal rate of tax ought to be brought down so as to make an effect; the decrease in the rate of tax collection should be at one stroke.

##### **2) Minimisation of controls and licenses**

A committee of professionals must be appointed to investigate the utilisation of all permit systems and existing controls and suggest which all are to be eliminated, whichever is not necessary. This committee must also be given the power to alter laws in such a way that these laws are healthy for the economy and which can be administered efficiently and effectively without any ill effects on the public.

##### **3) Regulation of donations to public parties**

Nowadays, it is very essential to keep political parties away from corruption. If selected with suitable criteria and evaluating the amount to be given to each one, it would bring about a huge change in this situation. Irrespective of whether the government funds the parties or not, their accounts must be checked on a regular basis showing all transactions important.

##### **4) Creating confidence among small tax payers**

The act of being too careful in small cases, when there is no advantageous revenue involved, has done a lot of harm to this division in general. The guidelines issued by the Central Board Of Direct Taxes on the new system for making evaluations in small income cases makes a bold departure from the past and are probably going to achieve more huge outcomes than the earlier small income schemes.

##### **5) Allowance of certain business expenses**

Entertainment expenditure incurred for the advancement of tax payers business which is directly identified with its dynamic direct have to be permitted to be deducted up to the segment 37(2A) of the Income Tax Act, 1961.

##### **6) Changes in penal provisions**

Penalty is needed just as much as it is within the sensible limit. Once it crosses that limit, it is bound to increment the inflexibility of the citizen's stubbornness than to reform him. A penalty that's dependent income rather than tax hits the small taxpayers more harshly.

**7) Intelligence and investigation**

To adapt to the expanding refinement and advancement of the procedures of tax evasion, there is a requirement for complete reorientation in the division's way to deal with its strategies of intelligence and investigation. The machinery for intelligence and investigation has to be completely upgraded and streamlined to handle sufficiently the hazard of tax evasion.

**8) Taxation of agricultural income**

Agricultural income which is presently outside the central tax net paves easy ways for camouflaging black money and it should be urgently subjected to a uniform tax which is more or less on par with other incomes so as to eliminate scope for evasion.

**9) Permanent account number**

It is necessary to index all the tax payers on a permanent basis reduces difficulties and confusions

**V. CONCLUSION**

Having known about the ill effects of tax evasion on our economy, it turns into every single one of our duty to help the government by conforming to the tax procedures and pay taxes immediately. Our little commitment will have a huge impact on the welfare of our economy and let us be the people who bring the change for the development and betterment. Tax evasion can be eliminated completely if we take the proper measures to fight it, further reducing the burden of payment on the existing payers. It is also important to further educate the people about the Indian Tax Laws and create an environment where everybody pays their dues efficiently and feel proud about their contribution to their economy.

**REFERENCES**

- [1]. Alm, J. (2012). Measuring , explaining , and controlling tax evasion : lessons from theory , experiments , and field studies, (August 2010), 54–77. <https://doi.org/10.1007/s10797-011-9171-2>
- [2]. Devarajappa. (2017). TAX EVASION IN INDIA : A STUDY OF ITS, (September), 134–138.
- [3]. Kang, M. (2016). A psychological perspective on tax avoidance : Deferential avoidance vs . defiant avoidance, 14(1), 235–246.
- [4]. Ministry of finance, A. (2016). Annual Report 2016-17.
- [5]. Spicer, M. W. (1974). Xerox University Microfilms DEL OF INCOM E TAX EVASION . The Ohio S ta te U niversity , Ph . D . , 1974 Economics , finance.
- [6]. Tarun, G., Jasmin, K. S. S., Sciences, T., & Sciences, T. (2018). A Study on Tax Evasion in India, 119(17), 219–225.
- [7]. <https://dea.gov.in/annual-reports/annual-reports-archive> - Audit report, Ministry of Finance