

Demonetisation, black money and GST



EXPERT EYE

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As the effects of demonetisation become clearer, we may assess its relation with black money and the goods and services tax (GST). Some economists have said demonetisation would not be so effective to check black money, as GST would be. I shall examine this proposition.

Let us first note that GST deals with indirect tax, the evasion of which makes black money. Other sources of black money are evasion of income tax and “black” deals in real estate.

With this background, let us see how much scope has remained to make black money in the set up of GST that has been worked out. The rates of duty are five per cent, 12 per cent, 18 per cent and 28 per cent. About five per cent and 28 per cent, there will not be much controversy if the items are listed properly. But, there will be fierce controversy between 12 and 18. I had suggested just 16, which would give same revenue and there would be no controversy as the tariff item could be described as, “other than those listed under five per cent and 28 per cent rates”. But, that has not been done. This may have been because of the pressure of the state governments. In any case, the tariff now being divided between 12 per cent and 18 per cent, the taxpayers will devise ways and means to pay less. And, some advisers with the intent to complicate the tariff will try to convince the government to introduce the CCCN. A senior lawyer has already started canvassing for that. If he is successful, the whole lot of con-

troversies with notes and explanations and definitions will come back. And, along with it, the existing level of corruption will also come back. So, the conclusion is that the way the GST has been done, there is as much scope of making black money as was there in the existing tariff.

Next, one must know that evasion is not uncommon in countries with GST all over the world, mainly in poorer countries, including in Europe. Like any tax, the value-added tax (VAT) is open to fraud and evasion. Many other evasion methods are common with other taxes such as retail sales tax (RST) and turn-over tax. There are, however, certain frauds which are distinctive to VAT. And, that is the input credit system. Evasion is done by criminals who evade tax on a mass scale. In the European Union and elsewhere, sophisticated VAT fraud, targeting its refund provisions, has become a

serious concern. Evasion of duty in different ways has become so serious a problem with VAT that the basic quality of VAT that it is self-correcting and self-enforcing can hardly be held as valid. In Netherlands (a rich country) the report of the survey on the Nature and Extent of Tax Evasion based on

77,000 field audits conducted in 1976 shows in 45,000 (more than 58 per cent) cases additional demand for tax evaded were issued yielding two per cent of the revenue of that year. The report said that fraud was slightly more frequent in the retail stage but revenue involved was less. The report estimated that if all returns were audited, 5.5 per cent (870 million guilders) revenue could be recovered. So, GST is not evasion proof. Black money will continue to be generated. The flow will not stop but one time demolition of black money by demonetisation has been a good step. The flow

would have been less had the rates of GST been five, 16 and 28 with very few exemptions.

The conclusion is that GST is not a substitute for demonetisation. It is partner of demonetisation in removing black money (by removing evasion of indirect tax only). GST does not affect black money generated by evading income tax and tax on real estate. GST is also designed to create an all-India market and promote ease of business. That would surely make more people pay tax voluntarily that would lead to greater collection of revenue and improve the tax GDP ratio and growth. So it is wrong to say that GST is better than demonetisation. They are complementary to each other and not substitute of each other. Demonetisation knocks out the stock of black money while GST stops the flow of it. Singly, none is so effective but jointly they are surely more effective.

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