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EXAMINING THE RELATIONSHIP BETWEEN MONEY LAUNDERING, TAX EVASION AND TAX HAVENS: A CRITICAL ANALYSIS

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I. Abstract

Criminal organisations undermine the rule of law and equality before the law by engaging in tax avoidance, tax evasion, and money laundering by multinational corporations and rich individuals. Furthermore, it magnifies social inequities and puts public services at risk. If everyone fails to comply with their tax duties, it is an attack on core concepts of equality, tax justice, democracy, and the rule of law. So, in this paper I'll be discussing the basic concepts of what amounts to as money laundering, tax evasion and tax havens and how they are somehow inter-connected. Also, some of the landmark cases, to have a better idea of the problem standing before us in the corporate world. As a final point, I plan to draw out a deduction made out of the former analysis.

II. Introduction

Money laundering is a very complexly vast topic, which requires a flexible and analytical political response to it. The present paper will only deal with the relationship between money laundering, tax evasion and tax havens. This is done with the tacit understanding that a narrow approach to anti-money laundering can only result in a concentration of criminal activities to those means that remain inadequately regulated. In other words the channels for money laundering function as communicating vessels where money can flow from one area to all the rest and as such only a holistic approach to anti-money laundering can be effective.

Money laundering is a criminal offence aimed at presenting wealth of illicit origin or the portion of wealth that has been illegally acquired or concealed from the purview of tax and other authorities, as legitimate, through the use of methods that obscure the identity of the ultimate beneficiary and the source of the ill-gotten profits.¹ It is a criminal offence whose consequences are usually detrimental to a polity's functioning and harmful to the socioeconomic fabric, both at domestically and overseas. Laundering money can take place in a variety of ways, including the shrewd exploitation of a complex, interweaving web of secrecy jurisdictions and/or tax havens, the manipulation of the concept of legal persons and legal arrangements to concoct 'shell companies'² that can act as covers for corrupt individuals, the abuse of loopholes in existing anti-money laundering legislation, the weak implementation of these rules, and the corruption of officials; in developed economies, this is mixed with the profiteering culture of several established financial

¹Samridha Neupane, *Money laundering*, LEGAL SERVICES INDIA, <http://www.legalservicesindia.com/article/436/Money-Laundering.html>

²Mr Rui Tavares, *Relationship between money laundering, tax evasion and tax havens*, SPECIAL COMMITTEE ON ORGANISED CRIME, CORRUPTION AND MONEY LAUNDERING (Jan., 2013), https://www.europarl.europa.eu/meetdocs/2009_2014/documents/crim/dv/tavares_ml_/tavares_ml_en.pdf

institutions and market insiders. Regardless of where the money came from, whether it was obtained through illegal activity or a criminal offence, the conduits for money laundering are virtually the same.

III. Money Laundering – The Dark Side

Money laundering is the illicit technique of making significant sums of money obtained through criminal activities, such as drug trafficking or terrorist financing, appear to have originated from a legitimate source. The proceeds of illicit activities are deemed "dirty," thus the process "launders" them to make them appear clean.³ Money laundering is a significant financial crime committed by both white-collar and criminals on the street. To detect and prevent money laundering, most financial institutions have anti-money laundering (AML)⁴ policies in place.

Anti-money laundering (AML) aims to deprive criminals of the revenues generated by their unlawful businesses, removing the primary incentive for them to engage in such criminal activity. Drug trafficking, people smuggling, terrorism funding, smuggling, extortion, and fraud are all illegal and dangerous activities that put millions of people in peril around the world and cost society a lot of money. Money laundering legitimises the proceeds of such activities, so combating money laundering may result in a reduction in criminal activity and thus a significant benefit to society.

Money laundering usually consists of three steps: placement, layering, and integration.⁵

- o The "dirty money" is secretly injected into the legitimate financial system through placement-

The bank account is usually opened in the name of a corporation that has been set up specifically for the aim of laundering money, with the help (either willingly or subconsciously) of experts such as lawyers. These corporations or businesses are referred to as "fronts" because their respectable look hides the criminal operations that generate the proceeds.

A series of individuals then make little cash deposits into the bank account on a regular basis.

The sums are always small enough to go below the bank's declared criteria, ensuring that no additional due diligence checks are performed. When the money is withdrawn or used

³*Money Laundering, Proceeds of Crime and the Financing of Terrorism*, UNODC, <https://www.unodc.org/unodc/en/money-laundering/index.html>

⁴Financial Industry Regulatory Authority. "Anti-Money Laundering (AML).", <https://www.finra.org/rules-guidance/key-topics/aml>.

⁵James Chen, *Money Laundering*, INVESTOPEDIA (Feb 25, 2022), <https://www.investopedia.com/terms/m/moneylaundering.asp#citation-2>

to buy other assets, it loses some of its criminal roots because it is now in a legitimate corporation.

- o Through a sequence of transactions and bookkeeping procedures, layering conceals the source of the money-

The second stage of the money laundering process is "layering." The funds are transformed or shifted away from the original source by purchasing genuine assets such as real estate. The asset is then sold to a reputable third party who is typically unaware of the situation. This stage is frequently repeated, with the proceeds appearing slightly more legitimate than they really are each time.

- o The now-laundered money is removed from the real account in the final phase, integration, and used for whatever reasons the crooks have in mind-

Some say that integration, the final stage of the money laundering process, was the only stage of Meyer Lansky's operations that he failed to complete. The proceeds are injected into a genuine economy at this point. The most prevalent scenario is where the proceeds are invested in a legal business with a high cash-based sales volume (ie, a casino). As a result, the proceeds are eventually cleansed, and they are said to shed all traces of their criminal origins. The original action can eventually yield a profit.

Note that this template may differ in real-life scenarios. Money laundering may or may not involve all three processes, or some of them may be merged or repeated multiple times.

However, some argue that no matter how many times the three-stage method is used, "dirty" money, or money related with illicit acts, can never lose its criminal origins. The reason for this is that proceeds do not vanish. They simply alter their look and form, making it more difficult to track them down. In the end, money earned by criminal behaviour has more restrictions than "clean" money. It can only be invested in or spent on activities that are less visible and profitable. There's always a chance that the proceeds will bring investigators back to the source of the crime and/or the perpetrator (s).⁶

Cryptocurrencies In Money Laundering-

Convertible virtual currencies (CVCs)—another word for cryptocurrencies—have risen to become the money of choice in a wide range of online illegal operations, according to the US Financial Crimes Enforcement Network (FinCEN) in a June 2021 report.⁷

⁶*Money Laundering*, ANTI MONEY LAUNDERING FORUM, https://www.anti-moneylaundering.org/money_laundering.aspx

⁷Financial Crimes Enforcement Network. "Anti-Money Laundering and Countering the Financing of Terrorism National Priorities," https://www.fincen.gov/sites/default/files/shared/AML_CFT%20Priorities%20%28June%2030%2C%202021%29.pdf

CVCs are increasingly being used to layer transactions and obscure the origin of money earned from criminal activities, in addition to being the favoured method of payment for buying ransomware tools and services, online exploitative content, drugs, and other illegal commodities online. Criminals use a variety of money-laundering strategies involving cryptocurrencies, including "mixers" and "tumblers," which disrupt the link between a sending address (or crypto "wallet") and a receiving address.

Indian scenario of money laundering-

Certain wise banking practises exist in India, which help to prevent the spread of money laundering activities in the country. The following are some of these practises.

- o Identification of prospective clients is carried out prior to the opening of a bank account by obtaining proper introduction. This procedure partly addresses the requirement of KYC.⁸
- o Criminal investigation is allowed in banking transactions in India. For example, the Income Tax Department can call for information relating to customers accounts and transactions. Erring accounts can be frozen. This addresses the Basle Principle on Compliance with legislation and law enforcement agencies.
- o Certain statues such as "The Bankers Books Evidence Act, 1891" and the "Banking Companies (Preservation of Records) Rules, 1985" require the making available / retention of records to investigating agencies, which addresses the Basle Principle on Record Keeping and Systems.

Cases-

- o **CHIDAMBARAM VS. DIRECTORATE OF ENFORCEMENT**⁹

FACTS - The case was before the High Court of Delhi from where the Appellant filed an appeal against the judgment in Bail Application No. 2718 of 2019 in Supreme Court by Special Leave where Section 439 of Code of Criminal Procedure, 1973 was allowed by the Supreme Court and the judgment of Delhi High Court dated 15.11.2019 was set aside. M/s. INX Media Private Limited wanted permission of Foreign Investment Promotion Board (FIPB) for issuing by way of

⁸In order to comply with regulatory provisions under the Prevention of Money Laundering Act 2002, Rules issued thereunder and related guidelines/circulars issued by SEBI, KYC formalities are required to be completed for all Unit Holders, including Guardians and Power of Attorney holders, for any investment (whether new or additional purchase)

of Rs. 50,000 or more in mutual funds. For the convenience of investors in mutual funds, all mutual funds have made special arrangements with CDSL Ventures Ltd. (CVL), a wholly owned subsidiary of Central Depository Services (India) Ltd. (CDSL)). See <http://www.amfiindia.com/showhtml.asp?page=kyc>

⁹P.Chidambaram Vs. Directorate of Enforcement, MANU/SC/1670/2019 [Criminal Appeal No. 1831 of 2019 (Arising out of S.L.P. (Criminal) No. 10493 of 2019)].

preferential interest, non-cumulative, equitable and convertible for engaging in business for operating, creating of bouquet of television channels. Further, the company also required permission for making downstream investment to the limit of 26% as well as the outstanding equity capital of M/s. INX News Private Limited. FIPB suggested for consideration and permission of Finance Minister. The Board did not approve the downstream investment. FIPB unit issued a press release dated 30.05.2007 which included the details of proposals which was approved in the meeting, in which it showed that the NRI inflow against M/s. INX media was Rs. 4.62 crores. Disagreeing with the permission of FIPB the company intentionally made downstream investment which was to the extent of 26% capital of INX News as well as made more Rs. 305 crores Foreign Direct Investment in INX Media Ltd. against the allowed foreign inflow of Rs. 4.62 is the accusation. Further FIPB unit letter dated 26.05.2008 required detailed clarifications from the company. The company in order to prevent penal action entered into conspiracy with Mr. Karti Chidambaram (Son of Appellant). Allegations which was put on him was that he exercised his influence over the FIPB unit which to undue favour to the company. Thereafter covering the investment received M/s. INX News Pvt. Ltd. and M/s. INX News (P) Ltd. come up to FIPB and asked for approval to downstream investment which was positively considered and approved by Finance Minister. It was further stated Mr. Karti Chidambaram for the services which was done to M/s. INX Group, had received the payments for it and invoices of around 3.05 crores was raised in favour of M/s. INX Group in which Mr. Karti Chidambaram was having interests. The then Finance Minister name was not there in the FIR. From the above FIR, the Respondent i.e. Directorate of Enforcement registered a case under Section 3[17] of Prevention of Money Laundering Act, 2002¹⁰ which is punishable under Section 4[18] of the Act against the accused. On 23.07.2018 he was arrested by the Respondent, during that time the Appellant filed an anticipatory bail in ECIR case which was dismissed because the Appellant can obstruct in the investigation and such case is not a fit case. On 21.08.2019 Appellant was arrested in CBI case and he was in custody from that time and on 16.10.2019 by the Respondents stating that an amount was paid of around 3 crores at his instance to companies which were controlled by his son. After Appellant's bail was dismissed by the court he made an application dated 05.09.2019 praying for surrendering before the trial court which was also rejected.

JUDGMENT- Court is not much inclined in opening sealed cover even though such materials were received by Respondent. The Appellant's name was not there in the case but allegations was made against him by the co-accused. Since the anticipatory bail was declined previously the Appellant

¹⁰ The prevention of money laundering act. 2002,
<https://www.indiacode.nic.in/bitstream/123456789/2036/1/A2003-15.pdf>

was available for interrogation for more than forty five days. Further, if the Respondents required for further investigation he is bound to be present. Noticing the situation as well as considering the duration he was in custody the Appellant is entitled to grant bail. Further execution of bail bonds for a sum of Rs. 2 lakhs with two sureties of the like sum produced and also the passport to be deposited. Further he won't be tampering any evidence.

o **UNION OF INDIA vs. HASSAN ALI KHAN & ORS.**¹¹

FACTS- This case was brought before the Bombay High Court from where the Appellant filed an appeal against the judgment as well as order in Cr. Bail Application No. 994 of 2011 in Supreme Court by Special Leave and the judgment of Bombay High Court dated 12.08.2011 was set aside. The allegations made against the Respondents as well as the others are that they committed offence which is punishable under Section 4[20] of the Prevention of Money Laundering Act, 2002. The case is registered by the Deputy Director, Enforcement Directorate, Ministry of Finance and Government of India on 08/01/2007 on Directorate report on documents which was received by the Income Tax Department. Further the department made a search in the premises of Respondent No. 1 and found a sum of Rs. 88,05,000 in Peddar Road, Mumbai which was seized. There was various imported watches and jewellery was also found and seized. Thereafter, he purchased an expensive car which was worth Rs. 60,00,000 from one Anil Shankar and paid till then sum of Rs. 46,00,000 towards that purchase. He also transferred various amount to different persons from accounts which was held by him outside India. After further investigation Income Tax Department assessed his total income previous years came to Rs. 110,412,68,85,303/-. He was further issued show cause notice under the Foreign Exchange Management Act, 1999 for violation of Section 3[21] and 3A[22] of the Act for dealing and holding foreign exchange of US\$ 80,004,53,000 approximately Rs. 36,000 crores in Union Bank of Switzerland and various accounts in Zurich. After making inquiries it was found that Respondent No. 1 was holding three passports by submitting false documents. He also sold a diamond from collection of Nizam of Hyderabad and through sale proceeds in his account in Basel, Switzerland to the Barclays Bank situated in United Kingdom. Based on the above facts, Directorate of Enforcement arrested him on 7th March, 2011 and was produced before Special Judge, PMLA in Mumbai and was remanded in custody. Further in the order dated 11th March, 2011 the Special Judge rejected the prayer of Directorate of Enforcement and released him on bail. Since Public Interest Litigation was going on in Court and status report was required to be filed by the Directorate of Enforcement of this, when the Court was brought into notice that the Respondent No. 1 is released on bail then this court stayed the operation of bail and ordered to detain him in custody initially for four days. A bail was further prayed by Respondent

¹¹ Union of India vs. Hassan Ali Khan & Ors., [2011] 11 SCR 778.

No. 1 but the same was dismissed by the Special Judge. Challenging the order of Special Judge the Respondent filed Bail Application before the Bombay High Court and after hearing he was granted bail by the order dated 12th August, 2011. Further the Learned Additional Solicitor General referred the provision of Section 45[23] of the Prevention of Money Laundering Act, 2002 which states about the offences which make cognizable and non-bailable and provides that no person can be released on bail whose offence is punishable for a term of more than three years under Part A of the Act and the exceptions are a person whose age is below 16 years or woman or a person who is sick.

JUDGMENT-The High Court proceeded by the attempt which was linked by the prosecution of different passports with the functioning of the foreign bank accounts is not acceptable and failed to focus on other parts of the case. Further the total income of Rs. 110,412,68,85,303 which was been by Income Tax Department in Section 24[24] of the Act the Respondent no. 1 was not able to establish the same neither untainted property. Lastly, the way Respondent No. 1 obtained three passports in his name even after the original passport was directed to be deposited brings question that if released on bail the Respondent No. 1 will escape. Therefore, Appeal allowed and the judgment of Bombay High Court is set side and the bail is cancelled which was granted to Respondent No. 1.

IV. TAX EVASION- A COMPLICATED PROBLEM

Tax evasion is a criminal offence in which a person or company knowingly avoids paying their true tax liability. Those who are detected avoiding taxes are usually charged criminally and face severe fines.¹²

For a variety of reasons, tax evasion must be successfully tackled. Initially, it prevents states from earning enough revenue, limiting them from enacting social, economic, environmental, cultural, and other initiatives. Tax evasion undercuts the government's attempts to promote welfare and social cohesion; it inhibits it from fulfilling its social role. Furthermore, it damages individuals' belief in the methods and objectives of a legitimate, democratic government by undermining the credibility of democratic institutions. In a nutshell, it can foster feelings that lead to anti-social and anti-democratic attitude.¹³ Perhaps the most significant negative impact is on equity. A manufacturing worker who earns a wage is subject to taxation. For tax purposes, a restaurant worker who earns the same amount but receives a portion of his salary in tips does not report it. As a result, one bluecollar worker benefits while the other suffers. This is referred to as horizontal imbalance. A salaried employee in the organised corporate sector earns the same amount of money

¹²Julia Kagan, *Tax evasion*, INVESTOPEDIA (March 19, 2022), <https://www.investopedia.com/terms/t/taxevasion.asp>

¹³Krishnaraj Singh & Raj Vikram Singh, *Tax Evasion & Black money in India*, Vol-5 Issue-2, (2019)

stated because their earnings appear to be the same for tax purposes. The upshot might be an increase in tax rates or the application of distortive levies, setting off a vicious cycle of inefficiency and unfairness. The development of black money, which is a societal evil, is a major consequence of tax evasion on the government. The increasing growth of illicit money in our economy has serious and terrible repercussions.

Measures Taken Beforehand To Identify Beneficial Ownership And Prevent Tax Evasion-

The Indian government has taken several initiatives to combat tax evasion, as listed below. Tax evasion is considered a crime in India. The government imposes prosecution and penalties under various acts. The Income Tax Department has implemented a tax evasion reward scheme, which compensates those who report tax evasion. India and the United States recently signed an agreement to prevent Americans from evading taxes through Indian financial institutions. Persons in possession of black money can invest in special bonds under the Special Bearer Bond Scheme (Immunities and Exemptions Act, 1981). Another was the Voluntary Compliance Scheme (Amnesty Scheme).¹⁴

The government raised the tax bracket, lowered the deduction rate, and tightened lawful tax avoidance techniques. The Government has established the Tax Administration Reform Commission to undertake fundamental reforms to tax concerns in order to simplify and streamline tax procedures. Previously, India established a number of committees, including the Taxation Enquiry Committee, the Indian Tax Reforms Committee, and the Direct Taxes Enquiry Committees, among others. The Finance Bill introduced the Transfer Pricing Audit to audit concealed transactions in order to combat tax avoidance.

Banks play a critical part in a country's economic development. They serve as pillars in finding tax evaders, disseminating information, and collecting taxes. They serve as a mediator, thus the Income Tax Department assigns responsibilities and liabilities to banks in order to combat tax evasion. The government is currently highly active in formulating policies and taking steps to ensure that they are carried out smoothly.¹⁵ From legal tender currencies to cash deposits in banks to faceless assessments and appeals, a lot has changed. The government is pushing toward digitalisation and ensuring that corruption is reduced at all levels.

¹⁴Sunil Kumar, *Tax evasion and controlling tax evasions by Indians*, LEGAL SERVICES INDIA, <https://www.legalserviceindia.com/legal/article-3728-tax-evasion-and-controlling-tax-evasion-by-indians.html>

¹⁵Divya Agrawal, *Roles & Responsibilities of Banks Increased by Income Tax Departments*, TAXGURU (March 01, 2021), <https://taxguru.in/income-tax/roles-responsibilities-banks-increased-income-tax-departments.html#:~:text=Banks%20play%20a%20vital%20role,tax%20evasion%20can%20be%20reduced.>

Recent Cases Of Tax Evasion In India-

In the fiscal year 2018-19, the Goods and Service Tax (GST) department registered around 1,470 cases of tax evasion and recovered over Rs 360 crore in Gujarat.

In connection with its tax evasion and benami assets investigation of Haryana Congress politician Kuldeep Bishnoi, the Income Tax Department has seized paintings worth Rs 30 crore.¹⁶

The raids to uncover the major tax evasion nexus were carried out in the first week of November on 42 locations across Delhi, Mumbai, Hyderabad, Pune, Agra, and Goa on a group of persons who were creating phoney bills and conducting Hawala transactions. Hawala is a term that refers to money transactions that take place outside of regular banking channels.

The Fight Against Money Laundering And Tax Evasion Has

Societal Implications-

Civil society, in general, and in particular those groups or sectors, such as journalists, NGOs, and academia, which all perform the benign duty of balancing, analysing, and checking authority, must provide an additional line of defence or examination.

Social partners should be rewarded for monitoring the application of all norms and detecting any violations, as well as receiving complete protection from censorship and politically motivated prosecution. Investigative journalism is critical in this sense, as it serves to not only expose existing crime or wrongdoing, but also to avert future crime. Investigative journalists' sources should always be kept confidential in order to avoid jeopardising ongoing investigations and discouraging future ones.

In contemporary times of technological and economic transition, proactive support for investigative journalism should be seen as a positive outcome, especially in terms of reducing crime and corruption. Furthermore, whistleblowers or non-governmental organisations (NGOs) working to expose bribery and corruption, government incompetence, and/or private-sector malpractices should be afforded the necessary protection and support at all times.

Money laundering and tax evasion-

Taxes play an important role in ensuring social equality. When it comes to the order of public services and social justice concerns in the country, paying taxes is a must. Failure to pay taxes is a defiance of fundamental concepts such as equality and democracy. On compelled institutions, tax evasion, tax avoidance, and money laundering issues are rarely addressed thoughtfully.

¹⁶ Income Tax dept seizes Rs 30 cr paintings in tax evasion probe against Kuldeep Bishnoi, THE ECONOMIC TIMES, Sep. 20, 2019

Furthermore, collaboration between law enforcement and anti-money laundering organisations is ineffective. As a result, the system becomes vulnerable.¹⁷

Money laundering is the most common method of evading taxes by concealing the source and amount of income. Money laundering is the practise of disguising illegal income from organised crime as legitimate income or erasing all proof of income. Money laundering routes serve as communication channels for money to migrate from one area to another, hence only a comprehensive approach to combatting money laundering is feasible. Money laundering is a criminal offence that aims to properly display some of the income that has been illegally acquired or hidden from tax and other authorities by utilising tactics that mask the identity of the eventual beneficiary.

By comparing the definitions of tax evasion and money laundering, the following similarities were discovered: both are illegal actions; both require breaking the law; both include deliberate conduct; and both conceal or disguise the money received. Because it has been commonly maintained that the proceeds of tax evasion are different from the proceeds of conservative criminality, it was important to examine the definition of tax evasion in terms of a crime.¹⁸

Examining the reasons why criminals launder money is another technique to demonstrate a link between tax evasion and money laundering. They are attempting to conceal wealth; they are attempting to cheat taxes in order to boost profits; they are attempting to legitimate the money; and they are attempting to avoid prosecution.

To establish the link between money laundering and tax evasion, consider some of the repercussions of money laundering. To begin with, money laundering undermines financial systems by increasing the portion of a country's economic activity that comes from sources that are lawful or illegal and fall outside of the country's commerce norms and regulations. Second, it encourages crime by allowing criminals to effectively use and deploy illegal funds. Finally, money laundering diminishes income and control by reducing government tax revenue and eroding government control over the economy, resulting in 'damage' to the general people.

¹⁷Money laundering and tax evasion, SANCTION SCANNER (March 31, 2021), <https://sanctionscanner.com/blog/money-laundering-and-tax-evasion-380#:~:text=Money%20laundering%20is%20the%20best,erase%20evidence%20of%20income%20altogether.>

¹⁸Ansia Storm, *Establishing The Link Between Money Laundering and Tax Evasion*, Vol. 12 No.11, (2013)

V. Tax Havens- A National Threat

Tax havens aren't always free of taxes. They normally levy a tax rate that is far lower than that of other countries. They frequently make up for the revenue loss through other means, such as raising import taxes, customs, and other fees. They may also demand large, even recurrent costs for company registration and other fees, such as licence fees. The government normally compensates for the revenue lost as a result of lower tax rates by doing so.¹⁹

Tax havens have been dubbed "global black holes," where the wealthy and powerful hide their wealth. When tax havens are portrayed this way, they appear to be completely illegal institutions meant to please the wealthy rather than foster growth, which is one of the primary goals of tax collection. This isn't fully accurate, though.

The principle of "Sovereignty" is the cornerstone of Public International Law. This implies that each sovereign nation has sole authority over its internal affairs and legal system. This means that a nation's decision on whether or not to charge tax, as well as the amount of tax it will levy, is solely its own. Thus, this system of creating a tax haven is not illegal by itself.

However, in this day of globalisation, it is quite easy to set up offshore shell firms, and many organisations utilise them to shift their earnings to tax havens for the sole purpose of dodging taxes, as seen in the example above. Such behaviour is illegal since it depletes the country's tax base, which is something that every responsible resident of that country is liable for. To combat this dilemma, numerous governments have signed treaties and Multilateral Instruments with tax havens to prevent illegal activities.

Tax Haven Criteria-

When determining whether a jurisdiction is a tax haven, the Organization for Economic Co-operation and Development (OECD) lists four important elements. The first is that no or only nominal taxes are levied by the jurisdiction. The absence of or nominal taxation is insufficient in and of itself to qualify a country as a tax haven.²⁰ The OECD recognises that each jurisdiction has the freedom to decide whether or not to levy direct taxes and, if so, at what rate. For a jurisdiction to be designated a tax haven, an examination of the other crucial elements is required. The following are the three additional elements to consider:

- ✓ Whether there is a lack of transparency-

¹⁹SohumDua, *How tax havens are regulated in India*, IPLEADERS (Sep. 11, 2020), <https://blog.ipleaders.in/how-tax-havens-are-regulated-in-india/>

²⁰Shashank Manish and Arun Soni, *Tax Havens and Money Laundering in India*, http://www.igidr.ac.in/conf/money/mfc-11/Manish_Shashank.pdf

There is usually more to a tax haven than meets the eye. A tax haven's legislative, legal, and administrative apparatus is opaque. There's always the possibility of behind-closed-doors secret judgements or negotiated tax rates failing the transparency requirement.

- ✓ Whether there are laws or administrative practices that prevent the effective exchange of information for tax purposes with other governments on taxpayers benefiting from the no or nominal taxation.-

Personal financial information is fiercely protected in tax havens. The majority of tax havens have official legislation or administrative policies in place to protect them from international tax authorities. There is no or limited information sharing with foreign tax authorities.

- ✓ Whether there is an absence of a requirement that the activity be substantial-

Outside entities are often not required to have a significant local presence in tax havens. A concession like this could lead to some fascinating circumstances. In the Cayman Islands, for example, one building held 18,857 largely overseas entities, according to a 2008 Government Accountability Office audit.²¹

This implies that by simply hanging your nameplate in a tax haven, you can claim tax benefits. Within the country's borders, there is no need to produce goods or services, or to conduct trade or commerce. Tax evaders can, for all intents and purposes, continue to do business in Florida while claiming to be Bahamas citizens when it comes to paying taxes.

Shell company explained-

A shell corporation is a legal entity set up in a tax haven to avoid paying taxes. Shell corporations usually only exist on paper, with no full-time staff and no physical location. Although the rules vary, many shell companies' true owners are not disclosed in their incorporation forms. Some people confuse the terms "shell company" and "offshore company."²²

Various questions come to our mind when we hear the word 'shell companies' like why are they called 'shell' companies? the basic answer to it is Because, like an empty shell, there is nothing inside. A shell company exists, legally, only on paper. Secondly, what are these shell companies used for? Their basic purposes are both legal and illegal. Shell companies can hold money, luxury homes, intellectual property, businesses and other assets. They also play a vital role in facilitating the flow of illicit money around the globe.

²¹Manoj Singh, *Tax Havens: All You Need Know*, INVESTOPEDIA (July 12, 2021), <https://www.investopedia.com/articles/tax/09/tax-havens.asp>

²²Will Fitzgibbon & Ben Hallman, *What is a tax haven? Offshore finance, explained*, ICIJ (April 06, 2020), <https://www.icij.org/investigations/panama-papers/what-is-a-tax-haven-offshore-finance-explained/>

Luxembourg : A Tax Haven For India-

Luxembourg is regarded as one of the world's biggest tax havens, as it draws a large amount of foreign direct investment. Luxembourg is the ideal destination to avoid paying taxes because of its low tax and inflation rates, thriving market economy, and focus on financial confidentiality.²³

The Tax Justice Network has Luxembourg placed sixth as one of the world's top enablers of financial secrecy. Luxembourg, on the other hand, no longer appears to be a paradise for tax evaders.

The DTAA between India and Luxembourg was updated in October 2019 to align with the OECD's BEPS Action Plan, significantly limiting the potential of tax evasion through foreign investment in Luxembourg. The "Principal Objective Test," as defined in Article 7 of the Treaty, examines the primary purpose of foreign investment or the formation of a company in another country for taxation purposes.

If it is determined that the primary objective of such investments and transactions is to escape taxes, the Treaty's benefits will be forfeited, and the investor's income will be taxed in India according to Indian law, therefore prohibiting tax evasion.

Government's Earning Through Tax Havens-

Tax havens aren't fully free of taxes. They have a lower tax rate than the rest of the world. To compensate for the loss of tax revenue, low-tax states typically levy hefty customs or import taxes. Tax havens may levy a fee for new company registrations, as well as annual renewal fees. Additional fees, such as licence fees, may be imposed. For tax havens, such fees and charges would add up to a periodic fixed income.²⁴

Even if they are only charged a modest tax rate, luring foreign persons or firms might result in the government earning significantly more tax money than it would otherwise. Furthermore, corporate investments in company operations that provide jobs for the country's citizens may benefit the government.

Money Laundering Using Tax Havens-

Money laundering is the act of converting criminal and corrupt gains into allegedly 'legal' assets, as well as the concealment of income and wealth from governments in order to avoid taxation.

Money laundering is a widespread practise that involves depositing 'dirty' money in a service company, layering it with legitimate income, and then integrating it into the flow of funds. Money

²³Yannick Hansen, *Luxembourg named in new tax haven investigation*, LT, Oct. 04, 2021, Online edition

²⁴*Tax Havens*, CORPORATE FINANCE INSTITUTE,

<https://corporatefinanceinstitute.com/resources/knowledge/other/what-is-tax-haven/>

earned by some crimes, such as extortion, insider trading, drug trafficking, and illicit gambling, is 'dirty,' and must be 'cleaned,' so that banks and other financial institutions will not suspect it.²⁵

Money laundering through tax havens usually takes the following forms:

- o Smuggling large amounts of cash to another country and depositing it in an offshore bank is known as bulk cash smuggling. The Bahamas, for example, are only 293 kilometres from Miami and may be reached by boat.
- o Trusts and shell companies: The true owner of the money is hidden via trusts and shell businesses.
- o Round-tripping: Money is put in a tax haven with few records retained, then sent back as a tax-free overseas investment.
- o Use of a digital currency conversion service to convert dollars into a digital currency that may be anonymously transferred and received. For a nominal cost, the receiver can convert the currency back to cash.

VI. Suggestions

- o It can be seen that because the activities involved in money laundering are international in nature, it is necessary to have a strong impact and that all countries enact strict and, if possible, uniform laws, because there will be no place left for money launderers to target for laundering their crime due to a lack of jurisdiction. There must also be procedures in place to ensure adequate cooperation between the state and the federal government. The conflict between the two must be resolved. Money laundering appears to be a victimless crime to the majority of people. Because of the negative consequences, it is now more important than ever to educate people about the crime and to be aware of money laundering cases. People will be able to notice the problem, which will help to better law enforcement because it will be open to public scrutiny. As a result, it is necessary to think nationally, globally, and regionally in order to have an effective anti-money laundering system.
- o High tax rates, corruption in public sector units, multiple tax rates and inefficient tax authorities are the main causes of tax evasion. It suggested that reduction in tax rates, simplifications of tax laws, remove loopholes in the tax system and some extent proper processing of information available the under the annual information return can be best tool for improving Indian tax compliance. Therefore there is a need for creating transparent, friendlier and less discriminatory administrative system. Further there is also a need to

²⁵*Tax havens*, TAXFITNESS (Dec 01, 2018, 11:45), <https://taxfitness.com.au/Tax-Havens/money-laundering-using-tax-havens>

educate the people about Indian Tax law and create such an environment in which they pay their due taxes, do not evade the tax and feel proud in discharging their duty to pay.

VII. Conclusion

Tax havens are small countries with affluent populations and well-developed governing systems. While all of these traits are linked to one another to some level, it is worth noting that poorly managed countries, of which there are many around the world, almost never emerge as tax havens. Their absence cannot readily be attributed to a desire on the part of badly governed countries to comply with international tax rules, because these countries aren't known for their compliance, and international tax norms aren't well established in the first place. Instead, the most plausible explanation is that tax havens fail in the absence of good governance, and because of this, poorly governed nations avoid attempting to become tax havens in the first place.

The study's conclusion is that, in addition to investigating money laundering, legal authorities should explore examining tax evasion. Although evidence from court cases suggests that the authorities may already be doing so, it may be more suitable to make it a formal part of their policy. The significance of this study is that it establishes a link between the crimes of money laundering and tax evasion. Although the evidence discovered in this study supports this assertion, it should be noted that nearly no literature linking money laundering to tax evasion could be uncovered.

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