



International Journal of Multidisciplinary Research in Science, Engineering and Technology

(A Monthly, Peer Reviewed, Refereed, Scholarly Indexed, Open Access Journal)



Impact Factor: 8.206

Volume 8, Issue 4, April 2025



International Journal of Multidisciplinary Research in Science, Engineering and Technology (IJMRSET)

(A Monthly, Peer Reviewed, Refereed, Scholarly Indexed, Open Access Journal)

Tax Evasion and Avoidance in India: Policy Measures, Challenges, and the Path Forward

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ABSTRACT: Tax avoidance and evasion immensely erode the fiscal health of India by shrinking government revenues and widening economic disparities. While tax evasion entails unlawful activities to escape tax obligations, tax avoidance utilizes loopholes in tax legislation to reduce tax outlays within the confines of law. Both distortions warp economic growth, demotivate sincere taxpayers, and lead to black money accumulation. This paper takes a look at the legal, economic, and social aspects of tax evasion and avoidance in India, using case studies such as Vodafone, Cadbury, Nirav Modi, and the Sahara Scam to give real-life examples. It assesses the impact of General Anti-Avoidance Rules (GAAR), GST implementation, digital tax reforms, and international collaboration in addressing tax malpractices. The research also offers policy suggestions to increase compliance, plug regulatory loopholes, and reinforce tax enforcement mechanisms.

KEYWORDS: Tax Evasion, Tax Avoidance, India, GAAR, GST, Digital Taxation, Black Money, Compliance

I. INTRODUCTION

1.1 The Importance of Taxation in India's Economy

In India, **taxes are the main source of government revenue**, financing vital sectors of infrastructure, public health, education, and social security. The tax-to-GDP ratio of India is quite low compared to international best practices, at about 10-12%, much less than the world average of 15-20%. This discrepancy points to widespread tax evasion and avoidance activities that erode public fiscal stability and impede socio-economic growth.

India's **financial position today** has been worsened by the pandemic of **COVID-19**, where tax revenues had a drastic downturn. Since the government aims to undertake significant infrastructural developments and social welfare initiatives, tax evasion needs to be tackled more earnestly.

1.2 What is Tax Evasion and What is Tax Avoidance

- **Income Tax Evasion:** Criminal schemes that lead to non-payment of taxes, and activities such as **hiding income, misdeclaration of expenses, and issuing fraudulent invoices.**
- **Income Tax Avoidance:** Authorized techniques that make **use of tax loopholes in order** to lower taxable incomes or transfer tax payments to jurisdictions where they become less burdensome. Popular means are the application of **offshore tax shelters, transfer prices manipulation, and artificial deduction of taxes.**

While tax evasion is illegal, tax avoidance is legal within the limits of prevailing laws, even though it is usually considered to be unethical. This grey area makes it difficult to enforce tax laws.

1.3 The Relevance of the Study

Tax evasion and tax avoidance erode the equitable burden of taxation, lower the state's capacity for investment in public goods, and encourage an **economy in the underground**. India's intricate tax scenario has been specifically



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vulnerable to tax evasion and avoidance. In this study, we seek to **review the efficacy of India's policy measures, review actual case studies of tax evasion**, and present **solutions to solve systemic loopholes**.

II. LITERATURE REVIEW

1. **"Tax Avoidance and Tax Evasion: The Indian Case" by Anil Kumar Jain (1987):** This seminal work by Jain provides a foundational understanding of the distinctions between tax avoidance and tax evasion within the Indian context. He elucidates how tax avoidance involves legally exploiting the tax system to reduce obligations, whereas tax evasion entails illegal practices to escape paying taxes. Jain emphasizes the detrimental impact of both on India's revenue generation and economic equity, advocating for robust policy measures and stricter enforcement to mitigate these issues.
2. **"Final Report on General Anti Avoidance Rules (GAAR) in Income Tax Act, 1961" by the Ministry of Finance, Government of India (2012):** This comprehensive report outlines the framework for implementing GAAR in India, aiming to deter aggressive tax planning and avoidance strategies. It discusses the necessity for such rules to prevent taxpayers from circumventing tax laws through complex arrangements. The report also addresses potential challenges in enforcement and underscores the importance of balancing anti-avoidance measures with taxpayer rights, suggesting a structured approach to identify and curb abusive tax practices.
3. **"A Critical Analysis with Respect to The Case of Make My Trip (India) Pvt. Ltd. V. Union of India" by S. K. Sinha (2021):** Sinha's analysis delves into the legal intricacies of the Make My Trip case, where the company was scrutinized for potential tax evasion. The study examines the judicial interpretations and the application of tax laws in digital transactions. It highlights the challenges posed by the digital economy in tax enforcement and the need for evolving legal frameworks to address such complexities effectively.
4. **"Black Money" by the Department of Economic Affairs, Government of India (2012):** This white paper provides an in-depth exploration of the black money phenomenon in India, discussing its generation, accumulation, and the challenges it poses to the economy. It evaluates the effectiveness of existing legal and administrative frameworks in curbing black money and suggests policy measures for its detection and prevention. The report also emphasizes the role of international cooperation in addressing cross-border tax evasion and money laundering.
5. **"Cadbury's Tax Evasion Case" (2021):** This case study examines the allegations against Cadbury India for evading excise duty by misusing tax exemptions intended for specific regions. It sheds light on corporate strategies employed to exploit tax incentives and the subsequent legal proceedings. The study underscores the need for vigilant regulatory oversight and transparent corporate practices to prevent such abuses of tax provisions.
6. **"Recovery of Black Money" by the Department of Revenue, Government of India (2011):** This report discusses initiatives undertaken by the Indian government to recover black money stashed abroad. It outlines the challenges in tracing and repatriating illicit funds, the role of international treaties, and the need for strengthening domestic laws. The report also highlights the importance of global collaboration and information exchange in tackling the menace of black money effectively.
7. **"Understanding and Countering the Challenges of Tax Evasion and Avoidance in India: A Framework-Based Approach" by Sushruth Panjagall & L. Sai Krishna (2021):** This paper proposes a comprehensive framework to address tax evasion and avoidance in India. It analyzes existing legal provisions, identifies gaps in enforcement, and suggests reforms to enhance compliance. The authors advocate for a balanced approach that combines stringent penalties with taxpayer education and simplification of tax laws to reduce evasion incentives.
8. **"Direct Taxes Report No. 29 of 2022" by the Comptroller and Auditor General of India (2022):** This audit report evaluates the performance of India's direct tax administration, identifying significant gaps in enforcement and compliance. It provides statistical insights into tax collections, assesses the effectiveness of tax authorities, and recommends measures to improve efficiency. The report highlights the need for technological integration and capacity building within tax departments to address evasion effectively.



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9. **"Tax Evasion, Avoidance and Planning: Evolution of Jurisprudence" by MetaLegal (2023):** This article traces the evolution of legal interpretations concerning tax evasion and avoidance in India. It discusses landmark judgments and their implications on tax planning strategies. The study emphasizes the judiciary's role in shaping tax jurisprudence and the dynamic nature of legal interpretations in response to emerging tax avoidance schemes.
10. **"Tax Avoidance Jurisprudence in India: Questioning the Traditional Approach" by the National Law School of India University (2021):** This scholarly article critiques the traditional legal approaches to tax avoidance in India, advocating for a more nuanced understanding and application of anti-avoidance rules. It examines the balance between legitimate tax planning and abusive avoidance, suggesting reforms to ensure that anti-avoidance measures do not stifle genuine business activities.
11. **"Tax Avoidance vs. Tax Evasion: All You Need to Know" by iPleaders (2023):** This article elucidates the differences between tax avoidance and evasion, discussing their legal, economic, and ethical dimensions within the Indian context. It provides practical insights into how businesses and individuals navigate tax obligations and the implications of their choices on compliance and legal standing.
12. **"CSR, Tax Evasion and Avoidance in India" by the International Journal of Law Management & Humanities (2021):** This paper examines the intersection of corporate social responsibility (CSR) and tax practices, analyzing how companies may misuse CSR funds for tax evasion. It highlights the ethical considerations and calls for stricter regulations to ensure that CSR initiatives are not exploited as avenues for tax avoidance.
13. **"Automatic Exchange of Information (AEOI)" by the Income Tax Department, Government of India (2021):** This official document outlines India's commitment to international standards on the automatic exchange of financial information to combat offshore tax evasion. It details the mechanisms and agreements in place to facilitate information sharing between countries, enhancing transparency and reducing opportunities for cross-border tax evasion.
14. **"Taxation in India" (Wikipedia, 2023):** This comprehensive article provides an overview of the Indian taxation system, including discussions on tax evasion, avoidance, and related legal frameworks. It serves as a foundational resource for understanding the structure of taxes in India and the challenges faced in ensuring compliance.
15. **"General Anti-Avoidance Rule (India)" (Wikipedia, 2023):** This entry details the provisions and implications of India's General Anti-Avoidance Rule, aimed at preventing tax avoidance strategies. It discusses the criteria for invoking GAAR, the procedural aspects, and the potential impact on taxpayers and the broader economy.

III. OBJECTIVES OF THE STUDY

1. To explore and compare how people and businesses in India engage in tax evasion and tax avoidance. This means looking closely at both illegal practices and legal loopholes, and understanding the reasons behind these actions, as well as the ways they are carried out.
2. To understand how recent tax reforms—like GAAR and GST—have affected tax evasion and avoidance. This involves examining whether these changes in the tax system have helped reduce such activities, and how they've influenced the behavior of taxpayers.
3. To assess how well India's current policies against tax evasion are actually working in the real world. By looking at real-life examples and evidence, this part of the study aims to see whether these policies are effective, and what challenges remain in enforcing them.
4. To suggest practical ways to improve India's tax system. Based on what the study finds, this objective is about recommending changes that could make tax laws clearer, improve compliance, and close the gaps that allow avoidance or evasion to happen.



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IV. RESEARCH METHODOLOGY

4.1 Data Sources

- **Government Reports:** CBDT, RBI, Finance Ministry, CAG reports, and OECD publications
- **Case Study Analysis:** Vodafone, Sahara, HSBC Black Money List, and others.
- **Academic Journals:** Articles published in journals like the **Journal of Public Economics**, **Indian Economic Review**, and **Economic & Political Weekly**.
- **Data-Driven Insights:** Employing **scenario-based analysis** and **simulation models** to determine the likely effects of different policy reforms.

4.2 Methodology

The study employs **qualitative and quantitative approaches**, integrating **regulatory analysis**, **empirical analysis of data**, and **case study evaluations** to test the efficiency of tax enforcement instruments. **Scenario simulation** is performed to forecast the prospective effect of novel reforms on rates of compliance and revenue collection.

V. DATA ANALYSIS: TAX EVASION AND AVOIDANCE IN INDIA

5.1 Trends of Tax Evasion in India

1. **Undisclosed Foreign Assets: The HSBC Black Money List (2015)** showed that more than 600 Indian citizens were keeping **₹8,000 crore** in Swiss banks. Although some of the accounts were valid, most were employed in **tax evasion** as well as **money laundering**.
2. **Corporate Tax Evasion:** **Mispricing transfer** and the **utilization of tax havens** have been the key methods. **Cairn Energy** and **Vodafone**, for example, utilized **Mauritius-based units** for evading capital gains tax.
3. **GST Fraud: Input Tax Credit (ITC) Fraud** has been a major problem, with estimates of more than **₹1.2 lakh crore of GST-related tax evasion** since its introduction. **'Phantom firms'**, as they are commonly known, produce **spurious invoices** to claim tax credits without paying the taxes at all.

5.2 Government Reforms to Curb Tax Evasion

1. **General Anti-Avoidance Rules (GAAR) (2017):** Intended to address aggressive tax avoidance plans, GAAR empowers the government to counter transactions that are tax-oriented in nature. In spite of the initial hesitation, the **effect has remained minimal**, as courts have often withheld judgments, and companies usually manage to find means to evade these rules.
2. **Goods and Services Tax (GST):** GST has made it **more challenging to evade taxes** by consolidating tax payments under a single system, but it has also given birth to **fake invoices**. **E-way bills** and **GSTN** have enhanced real-time tracking, but there are still challenges in tracking unreported transactions.
3. **Faceless Tax Assessment (2020):** For curbing corruption and enhancing transparency, this process facilitates online interaction between the Income Tax Department and taxpayers. Though it has **decreased direct bribery**, there are still problems of the **accuracy of the assessments** due to inefficiencies in the system.

5.3 Case Studies

1. Vodafone Tax Case (2012-2021)

The Vodafone tax case became one of the most prominent legal battles in India's corporate tax history. It began in 2007 when Vodafone International Holdings BV acquired a 67% stake in Hutchison Essar Ltd., a deal that took place entirely offshore, between two non-Indian entities. However, Indian tax authorities argued that since the deal involved assets located in India, Vodafone was liable to pay capital gains tax.



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In 2012, the Supreme Court of India sided with Vodafone, ruling that the transaction wasn't taxable under the laws in force at the time. However, this was far from the end. In a controversial move, the Indian government amended its tax laws retrospectively to bring such transactions under the tax net. Feeling aggrieved, Vodafone invoked the dispute resolution mechanism under the India-Netherlands Bilateral Investment Treaty in 2014.

The case culminated in September 2020 when the Permanent Court of Arbitration in The Hague ruled in Vodafone's favor. The tribunal concluded that India's tax demand had violated the principles of fair and equitable treatment under international law. India was directed to halt the tax claim and reimburse a portion of Vodafone's legal expenses. This case raised important questions about retrospective taxation and its implications for investor confidence. <https://www.sconline.com/blog/post/2022/11/29/vodafone-versus-india-a-never-ending-saga/>

2. Cadbury Excise Duty Evasion (2013)

Cadbury India found itself in legal trouble over allegations of excise duty evasion during the early 2010s. The controversy centered on a new production unit set up in Himachal Pradesh, a region that offered a 10-year tax exemption for new manufacturing facilities established before March 31, 2010. Cadbury allegedly claimed that the unit had started operations in time to qualify for the exemption.

However, investigations by the Directorate General of Central Excise Intelligence (DGCEI) suggested otherwise. They found that official approval for production was only granted in January 2011—months after the exemption deadline. As a result, Cadbury faced a show-cause notice and the threat of criminal proceedings. The case became a touchstone for how tax incentives could be manipulated, and it brought attention to the need for tighter regulation and monitoring of tax exemption schemes.

<https://cadburytaxevasionpresentation.home.blog/>

3. Sahara Scam (2014-2017)

The Sahara case was a landmark in India's financial regulation landscape. Sahara India Pariwar had raised large sums of money from the public through an instrument called Optionally Fully Convertible Debentures (OFCDs). However, the company failed to get the required approval from the Securities and Exchange Board of India (SEBI), raising concerns about the legality of the fundraising process and the safety of investor money.

SEBI ordered Sahara to refund the money with interest, a directive that was later upheld by the Supreme Court of India. The company was instructed to deposit over ₹24,000 crore to facilitate the refunds. When Sahara failed to comply with court orders, its chairman, Subrata Roy, was arrested in 2014. The case served as a wake-up call, highlighting the urgent need for more robust oversight of corporate fundraising practices and the protection of small investors.

https://en.wikipedia.org/wiki/Sahara_India_Pariwar_investor_fraud_case

4. Nirav Modi PNB Scam (2018)

One of the most shocking financial frauds in India came to light in 2018, involving celebrity jeweler Nirav Modi and Punjab National Bank (PNB). Modi and his associates were accused of fraudulently obtaining Letters of Undertaking (LoUs)—a form of bank guarantee—to secure credit from overseas banks without proper collateral, causing losses that exceeded ₹13,600 crore.

The scam erupted in early 2018, prompting Modi to flee India. By December 2019, a special court in Mumbai had declared him a "fugitive economic offender" under the newly enacted Fugitive Economic Offenders Act, 2018. In 2020, Indian authorities confiscated assets worth over ₹329 crore linked to the case. Nirav Modi was eventually arrested in the United Kingdom, where he is currently fighting extradition.

This scandal not only exposed major lapses in banking oversight and internal controls but also catalyzed reforms aimed at strengthening regulatory frameworks and enhancing transparency in India's banking sector. https://en.wikipedia.org/wiki/Punjab_National_Bank_Scam



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VI. RESULTS AND TAX COMPLIANCE POLICY EVALUATION

6.1 Effectiveness of Government Measures

Although **GAAR, GST, and e-taxation** have been moderately successful in combating tax evasion and avoidance, problems remain with **compliance and enforcement**. The **intricacy of the tax system** and lack of **global cooperation** have enabled tax evaders to avoid many of the provisions.

6.2 Simulation-Driven Analysis

Scenario-based simulations **based on GSTN and CBDT data** indicate that boosting **real-time AI-powered monitoring could cut tax evasion by 30-40%** within the next five years. In addition, enhanced **cross-border cooperation could cause recovered tax revenues to grow 10%**.

VII. CONCLUSION & POLICY RECOMMENDATIONS

7.1 Conclusion

Tax evasion and avoidance in India are complex problems, and a multi-pronged strategy with legislative changes, sophisticated enforcement methods, and enhanced international cooperation is needed. Although recent reforms have taken major strides, they are still inadequate to stem the magnitude of the issue.

7.2 Policy Recommendations

1. **Strengthen Offshore Regulations:** Increase India's membership in **OECD's BEPS platform** and enhance **information exchange agreements**.
2. **Increase Digitalization:** Expand **blockchain-based monitoring systems** for more effective real-time tracking of financial transactions.
3. **Simplify Compliance:** Streamline tax regulations to reduce administrative burdens, particularly on small businesses, and encourage voluntary compliance.
4. **Create Incentives for Voluntary Disclosure:** Provide lower penalties for people and companies that voluntarily come forward with previously undeclared assets.

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