16

MY REFLECTIONS ON THE INCOME-TAX LAW

It is said that tax systems reflect the values of a society.

Stiglitz, *Free Fall* p. 181

Here another great constant in economic life: as between grave ultimate disaster and conserving reforms that might avoid it, the former is frequently preferred.

Professor Galbraith

(1) Introductory comments

This Chapter and the next constitute a veritable potpourri of my ideas which developed in my mind over more than the three decades when I was a member of the Indian Revenue Service. I have called these Chapters as '*My Reflections*'. I am assertively present through them as a participative witness. These would surely not be so emotionally evocative as was Edmund Burke's *Reflections on the Revolution in France* (1789), but would surely provide you some ideas to reflect on the income-tax law as it has been administered in our country.

There are good reasons to think that the attitudes to tax law and its administration are determined by the dominant socio-economic ideas in changing times. The history of the western societies shows that the attitudes towards 'taxation' have generally been shaped by the dominant attitudes towards 'property'. But it is not possible to summarise them in this Memoir. In the history of income-tax, from the years of William Pitt in the *fin de sicle* of the 18th century to the neoliberalism of our times, it is clear that the attitudes towards 'taxation' have been shaped by the dominant interests in a political society. There was a time when Oliver Wendell Holmes could rebuke his Secretary who had exclaimed: "Didn't you hate to pay taxes!", with his hot response: "No, young feller, I like to pay taxes. With them I buy civilization." I was aghast at the Government of India's attitudes towards 'taxation', as reflected in the arguments advanced by our Government's Attorney-General Mr. Sorabjee before the Supreme Court in *Azadi Bachao's Case* [(2003) 263 ITR 706: AIR 2004 SC 1107]. His position can be gathered from what he himself wrote in his article dated 12 Oct. 2003 published in the *Indian Express:*

> "Thank God there is no patriotic duty to pay taxes which can be legitimately avoided unless, like the great Justice Holmes, one enjoys paying taxes, sharing his anachronistic belief that it is the price for the purchase of civilization. Tax practitioners and consultants would face serious problems if Justice Holmes is taken seriously."

The barbed tone reveals the neo-liberal ideas to which our government has allowed itself to be converted in the years after 1990s: the era, euphemistically called the era of 'opening up', when we are witnessing the GDP moving up, corruption increasing, values shrinking, and our Constitution shrivelling.

(ii) Taxation reflects values of a society, & attitudes towards 'property'

The present-day neo-liberal economic thinking holds rabid Lockean views[1] about 'property', which, bereft of all deceptive rigmarole, means that the government exists for the preservation of 'property'. We would surely find people who would better lose their life than their money, easier still to lose their soul than their property! Hubert Monroe is absolutely correct in saying: "The system introduced at the start of the nineteenth century shows every sign of being with us at the end of the twentieth".

I think it would help you to acquire a right perspective on the laws of taxation, statutory and also as judicially interpreted, if you keep in your mind the following changing views and shifting scenarios:

(i) Our ancient Indian thinking considered 'property' a thing under social trust for the welfare of people. Greed was considered a sin. I would refer to our classical attitudes towards 'property' in the Book III of this Memoir in the Chapter on 'My Reflections on Krishna & the Galaxy of the Great'. Ideas pertaining the imposition of just system of 'taxation' have been stated in the *Rig-Veda*, the *Mahabharata*, Chanakya and our classics.

(ii) But during the medieval India, the Turko-Afghan and the Mughal rulers, who had once been the cruel Turkish invaders, ruled us as the heartless imperialists for several centuries. They had embraced Islam for political reasons, not because they shared Islam's high democratic and egalitarian values. For them, 'taxation' was the most effective source for enriching the treasury of the emperors. The tax-gatherers had only the emperors to please, and to line up their own pockets. People, hated 'taxation' and the tax-gatherers. The historians have told us how the extortionate tax-gatherers brought the government itself into disrepute. Whatever was gathered through taxation became the emperors' property available for use or misuse. I have called this model of economy, that the medieval India's autocrats built, the 'Taj Mahal Economy' to which I would come again in Chapter 25 of this Memoir.

(iii) What I called the 'Taj Mahal Economy' is again in our sight these days. 'The fault, dear Brutus, is not in our stars,/But in ourselves, that we are underlings' (Shakespeare in *Julius Caesar*). Whilst our nation's common people (pejoratively dubbed by the economists as the *aam aadmi*) are reeling under severe price rise, and are starving, our government has no compunction in raising taxes, and reducing subsidies to push up prices of the essential goods. The recently held Commonwealth Games illustrates the present-day 'Taj Mahal Economy'.

(iv) It would be proper to illustrate how the present-day neo-liberal ethos has shaped the taxation policies. After 1991, we pampered and tolerated for diverse motives, not all honourable, the waves of foreign investors to frolic and play on our stock-market to reap profits, and to let them go out of the country without any let or hindrance. The watchers of our national interest allowed our tax treaties to be massively misused. Not only what was obvious was not being seen, steps were taken through administrative omissions and commissions to exclude transparency almost wholly. The climax of knavery was reached when the Indo-Mauritius Double Taxation Convention was allowed, with full knowledge of all those who mattered, to be turned into a Noah's ark for all the swindlers and masqueraders from different lands to fatten themselves with gains on the Indian Stock Market. The IMF taught us that if a red-carpet welcome was not given to foreign capital, it might go, never to return. Capital gains taxes, were cut down so that unearned super profits could be reaped through speculation. The American model and theory inspired us. Bertrand Russell perceptively said: "In the advanced countries, practice inspires theory; in the others, theory inspires practice." [2]

Popular, but perverse, attitudes towards taxation law

I can say that the attitudes towards taxation, which the ghosts held in W.S. Gilbert's comic opera *Ruddigore*; or, *The Witch's Curse*, are even now strongly shared by many. This is the mind-set which considers the evasion of taxes no crime. Almost a century after William Pitt, W.S. Gilbert portrayed in this opera, how common people looked at the breaches of income-tax obligations. Sir Ruthven Murgatroyd, Bad Baronet of Ruddigore, was cross examined by his ghostly ancestors who had obliged his descendants to commit a crime a day? That conversation is profoundly suggestive:

"Rob. Really : I've committed a crime punctually every day.

Sir, Rod : Let us inquire into this Monday?
Rob : Monday was Bank Holiday
Sir Rod : True, Tuesday
Rob : On Tuesday I made a false income tax return.
All : Ha! Ha!
1st Ghost : That's nothing.
2nd Ghost : Nothing at all.
3rd Ghost : Everybody does that.
4th Ghost : It's expected of you."

This is how the ghosts thought of the "evasion of taxes". If the ghosts can be so creative in accounting and the art of concealment, why shouldn't the living beings be enterprising in tax evasion. I had enjoyed this opera whilst a student at C.M. College. I had never thought that my destiny would drive me to see this real melodrama for more than thirty years as a member of the Indian Revenue Service!

(iii) How the British Judges fared when they came to have the tryst with the Income-tax Law

As the structure of the present income-tax law continues broadly the same as it was when it had been enacted in England during the Napoleonic Wars, the judicial approaches to the construction of its provisions have, with rare exceptions, remained fossilized, and largely stereotyped. In England the Judges could make their presence felt on the law of income-tax only from 1874. How did they respond to this new challenge? To quote Monroe again[3] :

> "As was said of the lion in the case of "Albert and the Lion" you could see that the judge did not like it. Here was a topic of which few, if any, judges had professional experience, though all no doubt had disagreeable personal experience The topic was entirely statutory, ...and apparently lacking in any discernible principles. What could a judge do but fall back on the words of so much of the statutory code as was brought to his attention."

How did the Judges fare, when construing the Income-tax Act? It reveals itself best in the ways the judges formulated the norms to govern the principles of statutory construction. More than 140 years have gone when Lord Cairns formulated the norms governing the construction of the statute in *Partington* v. *Attorney-General*[4] . The House of Lords decided certain issues which pertained to the law of probate duty. The issue did not relate to the law of taxation. What he said has become *locus classicus:*

> "As I understand the principle of all fiscal legislation, it is this: If the person sought to be taxed comes within the letter of the law he must be taxed, however great hardship may appear to the judicial mind to be. On the other hand, if the Crown, seeking to recover the tax, cannot bring the subject within the letter of the law, the subject is free, however apparently within the spirit of the law the case might otherwise appear to be."

The only rationale for such assertive formulation in such a wide sweep was the sanctity of 'property' rights. Lord Cairns himself brought out the rationale of his thesis. He said in *Pryce* v. *Monmouthshire Canel and Railway Co.*[5]

> "The cases which have decided that taxing Acts are to be construed with strictness and that no payment is to be extracted from the subject which is not clearly and unequivocally required by the Act of Parliament to be made, probably meant little more than this, that, in as much as there was not any a *priori* liability in a subject to pay any particular tax, nor any antecedent relationship between the taxpayer and the taxing authority could be brought to bear on the construction of the Act, and, therefore, the taxpayer had a right to stand upon a literal construction of the words used whatever might be the consequence."

It is difficult to understand why this literalist construction was preferred to the technique of discovering reasonable meaning. He must have been familiar with the idea set forth in Chapter 8 of Blackstone's *Commentaries,* edited by Edward Christian, which said:

> "It is considered a rule of construction of revenue acts, in ambiguous cases, to lean in favour of the revenue. This rule is agreeable to good policy and

public interest; but, beyond that, which may be regarded as established law, no one can ever be said to have an undue advantage in our courts."

And in 1899 in *Styles* v. *Treasurer of Middle Temple,* Justice Willis commented :

"I quite agree that every tax, if it is to be supported at all, must be found within the clear language of an Act of the Parliament, but I myself rather disposed to repudiate the notion of there being any artificial distinction between the rules to be applied to a taxing act and the rules to be applied to any other act. I do not think such artificial distinctions ever can help anybody in arriving at the true meaning of word."

(iv) The British courts adopt a new salutary perspective

But many eminent Judges of later times preferred the technique of purposive interpretation in the determination of meaning, a method which our *Mimansa* had developed and applied in ancient times. It took years for justice-oriented and welfare-mandated attitudes to develop to acquire judicial recognition. In *IRC v. Federation of Self-Employed*[6] , Lord Scarman explained the nature of the income-tax law, and pointed out the duties of the authorities administering the income-tax law. The following propositions follow from Lord Scarman's exposition in this decision by the House of Lords:

(i) In dealing with the affairs of tax payers the principles of fairness should operate.

(ii) The duty to collect 'every part of inland revenue' is a duty not owed exclusively to the Crown. It is a legal duty owed by the Revenue to the general body of the taxpayers without discrimination.

(iii) The duty of the Revenue is to "consider as one of several arising within the complex comprised in the care and management of a tax, every part of which it is their duty, if they can, to collect".

(iv) The success of tax avoidance scheme increases, *pro tanto*, the load on the shoulders of the great body of good citizens.

(v) To produce a sense of justice is an important objective of taxation policy.

(vi) The courts have a role, long established in the Public Law. There cannot be 'the retreat of the courts from this field of public law merely because the duties imposed on the Revenue are complex and call for management decisions in which discretion must play a significant role.'

In England this approach got a brilliant illustration in *Furniss* v. *Dawson*[7] which the House of Lords decided indicating in clear words that the elaborate schemes designed to minimize tax liability might in future be at the risk of being set aside at the instance of Revenue.[8] As usual the corporate world and its hired experts were ferociously up against that decision. It was only the maturity of the British polity that helped government not to bend, break, or succumb to pressures, overt or covert. I wish our courts adopt Lord Scarman's creative approach in deciding our tax cases so that the public interest is amply protected.

II

CERTAIN CHANGES IN THE STATUTE OF THE INCOME-TAX SUGGESTED

The Income Tax Act has become so complex that most often comprehension of many of its provisions becomes an exercise in utter frustration. Fundamental principles of the Income Tax Law are simple. Various statutory provisions are either illustrations thereof, or overriding thereon, or deviations therefrom. Many matters touching economic management, extraneous to the basic scheme of tax law, have been inserted in the tax-law when they could have been managed through separate enactments. The income-tax law tends to become bafflingly complex on account of the incorporation of the intricate concepts of property jurisprudence, criminal law, corporate jurisprudence, civil law and also on account of new commercial and financial products and inventions which have proliferated in recent years. This is time to think of a new morphology of the tax law, and to provide it a purposive coherence in plain English. Some points of importance are these.

(a) Apt illustrations to the legal provisions may be incorporated in the statute

H.W. Fowler, in the preface to the second edition of the *Concise Oxford Dictionary*, said: "define and your reader gets a silhouette; illustrate and he has it in the round". 'In the round' is a figurative expression which Fowler himself defined to mean: "with all the features etc. fully shown, all things considered". The Radcliffe Royal Commission struck a note of optimism. After much reflections, it made two salutary suggestions hoping that these would go a lot towards the simplification of the tax law. The Commission said with candour:

> "We do not feel satisfied that it is impossible to introduce greater clarity and concision into drafting of income tax legislation. The point is so often a matter of public criticism, and for more than a generation it has been a subject of judicial complaint....We remain under the impression that the possibilities of an improved technique are not exhausted and some advance could still be made in the way of clarity."

Two suggestions can be put forth for serious consideration : these are-

(a) to provide illustrations in the statute itself throwing light on the meaning of its complex provisions; and

(b) to recast the statute focusing more on the statement of principles, leaving many matters for the judges to decide on the general principles of justice (as is done in many civil law countries).

Illustrations have helped us to understand the provisions in many important statutes: *viz.* Indian Contract Act, 1872, and the Indian Evidence Act. "Illustrations are", says Mulla in his work on the *Transfer Property Act* (7th Edn.) "the practical application of the written law and make nothing law which would not be law without them." Mulla aptly cites a case from the *Straits Settlement* (*Mohomed* v. *Yeoh*[9]), in which the Privy Council said:

"The great usefulness of the illustrations which have, although not part of the sections, been expressly furnished by the Legislature as helpful in the working and application of the statute should not be thus impaired."

Our own Supreme Court has taken an analogous position in *Jhumma Masjid* v. *Kodimaniandra Deviah* AIR 1962 SC 847.

But till illustrations are introduced in the Income-tax Act, 1961, better-drawn leaflets and booklets deserve to be issued to help tax-payers to help them to get out of the labyrinths of the income-tax statute.

(b) 'Legislation in detail be abandoned, and replaced by legislation setting forth principles'

The above expressive heading tries to express what Lord Denning aptly said in his *The Closing Chapter* (at p. 112):

"Legislation in detail has been found by experience to be self-defeating. It leads to statutory provisions which are so complicated as to be obscure and unintelligible. When this happens, it offends the fundamental principle that a statute should be so expressed as to be readily understood by those who are affected by it….. legislation in detail should be abandoned and replaced by legislation in principle. By this I mean that our statutes should expound principles in clear language and should leave the details, where necessary, to be worked out by some other means or in some other way."

Lord Denning thinks that the gaps in the legislation could be filled by the judicial creativity. We have no reason to distrust that process. I have always felt that the Judges can be trusted to play this role well. Lord Denning has put this point felicitously: "They developed the common law in that way. They be trusted, likewise, with the statute law."

(c) The linguistic and thematic structure of the Income-tax Law

A periodic review of the Income-tax Act is always desirable. A comprehensive study of the income-tax law requires a study of its broad structure, which is simple. The Act is structured on the following protocol:

Protasis (the clause expressing condition)	*Apodosis (the consequent clause)*
'If' clause	'then' clause
If a particular legally protected interest is breached, or its prescribed conditions are violated	Then a particular consequence would follow as a matter of course which may involve declaration *simpliciter*, or punitive or compensatory actions.

In fact, there must be "if-then" (protasis-apodosis) relationship involved in a given legal provision. Besides being couched in the "if-then" relationship, the legal provisions are of various types needing differential treatment. They are the charging provisions, the machinery provisions; and the exculpating, ameliorative or exempting provisions. The present Income-tax Act is rich in provisions belonging to all these categories.

I remember when I was asked by someone quite well versed in the income-tax law: "Can't we frame single sentence Income-tax Act?" I said off the cuff:

"Why not? We may say:

Income at the rate prescribed in the annual Finance Act (or in the schedule annexed to it) shall be charged on the real income (accruing, arising or received) of every person."

Often I felt that if that were to happen, this law would work better. The word "income" would mean what it means "in a sense which no commercial man would misunderstand". This is what our Supreme Court said in *Calcutta Co Ltd* v. *CIT* (37 ITR 1, 9); and in scores of other Cases. My comment may seem extreme, but it invites you to reflect on the points suggested.

(d) Plain English would help

Right from the days, when I read as an undergraduate H W Fowler's *King's English,* and Gower's *Plain English,* I fell in love with Plain English, though in the years I served the Income-tax Department, I failed to live up to that standard. But I had my many moments when I was nonplussed by the gobbledegook of the tax law. We all must have seen a spider having its last laugh caught in the gossamer-web that it itself created. Both the tax-gatherers and the tax-payers have often lost their ways in the labyrinthine statutory provisions: where once one is in, one doesn't know how to get out of it. Lord Renton pointed out in his peroration at the end of his opening speech in the House of Lords, which Lord Denning has quoted in his *The Closing Chapter* (at p. 112) with approval:

"If our Acts of Parliament cannot be understood even by clever experts it not only brings the law into contempt, it brings Parliament into contempt. It is disservice to our democracy; it weakens the rights of the individual; it eases the way for wrongdoers and it places honest, humble people at the mercy of the state. In the name of reason and justice, let's get it straight!

And then goes Lord Denning: "To my mind, the one way to get it straight is for Parliament to use plain, simple language expressing principles, and for the judges to fill in the gaps in statutes as to do what good sense requires." High ideal might virtually be a quest for some El Dorado, but even a little advance towards the objective will spare us of much of our drudgery.

(e) Suggestion for constituting certain Committees for ongoing reforms

I have all along felt that there should be two permanent committees, one of our Parliament and the other of our eminent experts, to study and suggest measures for administrative and legislative steps in the matter of the tax law and its administration.

Considering the factors contributing to the complexity of the tax law, H.H. Monroe, who had the experience of having worked as the Presiding Special Commissioner in the United Kingdom, and had wide experience as a leading member of the British Tax Bar, suggests:

"Given goodwill, co-operation and a readiness to accept something short of perfection, measures to improve the existing law and such additions to it as are on mature reflection really necessary should not be difficult to achieve.

> Parliamentary procedures seem to hold the key; some sort of permanent committee, with experienced and expert assistance, to review existing and future legislation not just in relation to its content but in relation to its form seem to offer a practical expedient worth a try. Is the will lacking? Should we all shout together? We might be heard."

His rhetorical question must be answered: "YES".

It would be good if our Parliament establishes a Permanent Committee on Taxation on the analogy of the Committee on Treaties in Australia, and Canada. *Ad hoc* Parliamentary committee is not good enough. I may state that my study of our Parliamentary practice and procedure, with the *Parliamentary Practice of Erskine May* as my manual, has led me to conclude that our Parliamentary system of Committees, including those on Petitions, have not worked well in our country for reasons not appropriate for being examined here in this autobiographical Memoir.

The draft of the Income-tax Act, 1961 had been drawn up by an expert Committee consisting of P. Satyanarayan Rao, G.N. Joshi, N.A. Palkhivala, under the Chairmanship of M.C. Setalvad. They had drawn up the 12th Report of the First Law Commission (1958). In framing the Act, much was drawn from the Direct Taxes Administration Enquiry Committee Report (1959). These Reports were comprehensive enough to give us full ideas of the problems which Commissions and the Committees had considered. We knew that their authors were great masters of jurisprudence, possessed internationally recognized professional calibre, and integrity, and had wisdom and sagacity rarely noticed these days. Perish the thought, the Government must not give an impression that things are being engineered through stealth for ulterior purposes (which might include the unworthy practice of 'outsourcing' the drafting of the law to those who have their own interests to promote.).

III

The Role of Parliament in 'Taxation': and its *raison d'etre*

The most distressing point I have noticed, both as a member of the Indian Revenue Service for more than three decades, and as an Advocate for more than a decade at the High Court and the Supreme Court, is the general non-realization of the great constitutional fact that 'taxation' is, apart from being a method to raise resources, a most powerful way to subject the executive government to an effective democratic control through Parliament. *The New Encyclopedia Britannica*[10] aptly observed:

> "The limits to the right of the public authority to impose taxes are set by the power that is qualified to do so under constitutional law. ….. The historical origins of this principle are identical with those of political liberty and representative government – the right of the citizens."[11]

The nature and relevance of the Parliamentary control on 'taxation' generally, and the 'direct taxes' in particular, has been thus brought out by Hood Phillips[12]:

> "It was supposed to have been settled by Magna Carta and by legislation in the reigns of Edward I and Edward III that taxation beyond the levying of customary feudal aids required the consent of Parliament. One of the

> central themes of English constitutional history was the gaining of control of taxation and national finance in general by Parliament, and in particular the Commons; for this control meant that the King was not able to govern for more than short periods without summoning Parliament, and Parliament could insist on grievances being remedied before it granted the King supply. This applied at least to direct taxation…... [13]

In England even tax treaties are done only after getting Parliamentary approval. In England there is a system under which Parliamentary supremacy over the exercise of the executive power of treaty-making is maintained in the following two ways:

(a) by providing that a tax agreement is to be made only in terms of the law; and
(b) by providing that no tax treaty can be made without a Resolution by the House of Commons which has the exclusive control over taxation.

Parliamentary control on taxation is considered so important that in the major countries of the world the tax treaties (I mean, Double Taxation Avoidance Agreements), are done only with Parliamentary approval[14]. Over all the decades I served as a member of the Indian Revenue Service, I have found that, in our country, Parliamentary control on 'taxation' is seldom effective. Legislative provisions are enacted without meaningful deliberations in Parliament: they are mechanically enacted. I would reflect on our Parliament at work in the Book III.

It is distressing to see that the effective control of the Parliament through 'taxation' has waned despite our Constitution's provisions under Article 265 which excludes the imposition of tax (also by implication, the exemption from tax) without the authority of law.

Now one *reductio ad absurdum*. A close watch of the events show us how a new model for gathering resources for the Government is becoming available. It may be possible someday even to do away with Direct Taxes all together. It is possible to think that it would be enough to gather resources from the Indirect Taxes where the billionaires and the beggars are hit alike, and also from the grant of concessions, franchises, and by imposing charges for the rights to use the national resources. If in the process water resources are exhausted, riverbeds can be leased or auctioned. Already there is a move afoot to tax ground-water. Many new variants can be found or invented. Why not pollute 'air', or allow others to pollute it? If that happens, some MNCs would come to sell balloons with oxygenated air for people to buy in order to exist. The Government might become the beneficiaries of such corporate depredations by becoming their facilitators. And I heard a bird twitter from a bush: When all these are exhausted, human beings, not employable in the market, can become commodities for trade (see David Riesman's *The Lonely Crowd*), for which licence could be sold to some MNCs! This last idea is absurd, but we have seen many absurd things happening in the present-day Economic Globalisation. Like Cassandra, I am trying to see things yet in the womb of time: but I would be the happiest person if history proves me wrong in thinking this way.

Changing Judicial Perception of tax-evasion situations

On general overview of the judicial trends in the tax matters at our Supreme Court, I have perceived broadly three phases, each characterised by distinct features, though divergent tendencies often merge with shifting measure of emphasis. The phases can thus be identified:

(i) The Phase I: when the Right to Property was still a Fundamental Right, *i.e.* up to 1978;

(ii) The Phase II: when the organs of the State strove to carry out their Constitutional mission of socialism and egalitarianism; and

(iii) The Phase III: when law and justice are supposed to be 'market-friendly' as it is conceived and interpreted under the neoliberal paradigm of the present-day Economic Globalization.

The Phase I broadly pertains to the period when we still had the fundamental right to hold 'property'. During that period the judicial attitudes towards taxation resembled the conventional British attitudes towards taxation. It was based on the assumption that tax-payers had no social obligation, and was free to arrange their affairs if they could do so without offending the law. An excellent exposition of the characteristic features of this approach has been made by H. H. Monroe in one of his Hamlyn Lectures:

> "If social attitudes to evasion are tolerant, judicial attitudes to avoidance are ambiguous. Inevitably one judge will emphasize the citizen's right to arrange his affairs within permitted legal limits to avoid the incidence of tax.[15] Another will be critical of the expenditure of so much ingenuity and expertise in a pursuit so devoid of public benefit.[16] Yet a third will find the artificial pretences involved in many schemes worthy of censure.[17] Inevitably metaphors are introduced into the discussion of policy and of individual cases: "There is a certain fascination in being one of the referees of a match between a well-advised taxpayer and the equally well-advised Commissioners of Inland Revenue, conducted under the rules which govern tax avoidance. These rules are complex, the moves are sophisticated, and the stakes are high."[18] There can be few other branches of the law where the interaction of interests between community and individual is regarded as no more than a game."

The Phase II reached the apogee of its verve in the early 1980s when an excellent account of judicial creativity and activism was given by some of our most creative and activist judges: to mention the five who constituted a fraternity: they were Krishna Iyer, Bhagawati, Desai, Chinnappa Reddy, and later Justice Thakar. This approach, to the extent related to 'taxation', found the finest expression in the Constitution Bench judgment in *McDowell*[19], where Justice Reddy observed, (to which all other four Judges agreed):

> "The evil consequences of tax avoidance are manifold.... In our view, the proper way to construe a taxing statute, while considering a device to avoid tax, is not to ask whether the provisions should be construed literally or liberally, nor whether the transaction is not unreal and not prohibited by the statute, but whether the transaction is a device to avoid tax, and whether the transaction is such that the judicial process may accord its approval to it."

Justice Reddy approved the view of the activist Judges of the U.K. who felt that there could be situations where the judiciary could provide better remedies than the legislature. Lord Scarman observed in *Furnis v. Dawson*[20] :

> "Difficult though the task may be for judges, it is one which is beyond the power of the blunt instrument of legislation. Whatever a statute may provide, it has to be interpreted and applied by the courts; and ultimately it will prove to be in this area of judge-made law that our elusive journey's end will be found."

The Phase III is characterized by the narrowing of judicial role in this phase of globalization fostering the neoliberal economic paradigm. Two features, dear to the proponents of neoliberalism, are manifesting themselves in judicial approaches of our Supreme Court: these are[21] —

(i) the agenda to roll-back State activism in welfare measures, and aggressive cutback in the activities of government; and

(ii) the Government, through its policies, must be market-friendly, and it must ensure the promotion of the interests of big corporations which work by establishing a symbiotic relationship between the government and the business.

Writing about *A.D.M. Jabalpur* v. *Shivkant Shukla*, some experts observed: "The judgment can be best described, in the words of C.K. Allen, as the contribution of the Supreme Court to the emergency"[22]. With greatest humility, I feel that *Azadi Bachao Andolan*, about which I would tell you in detail in Chapter 23 of this Memoir, can be considered our Supreme Court's contribution to the Market Economy in this phase of Economic globalisation.

The justification for the annual Finance Act

I have often noticed how our Executive government considered the practice of enacting the Annual Finance Acts an irksome custom, best if done away with. But the rationale of the Annual Finance Act always impressed me as a powerful device to control the Executive. The Executive must come every year before Parliament seeking authorization to raise taxes. If it ever succeeds in getting a perpetual authority to raise taxes without coming to Parliament, it can easily turn despotic as was King James of England, or Chancellor Bismarck of Germany.

Besides, I always thought that what was needed most was transparency in the process. It would be good if the proposals of statutory changes and the budget proposals are placed in the public domain for well-informed discussion. There is nothing to lose, but everything to gain. I endorse fully the suggestion which emerged in the seminar on the 'Present State of Tax Statute Law' held in England in 1967. It was held under the chairmanship of Lord Scarman. One of the suggestions that emerged from it was:[23]

> "…..that the possibility of modifying the existing rules as to budget secrecy might be explored with a view to promoting discussion and consultation on the technical and legal aspects of tax legislation before it comes to Parliament."

Stiglitz has graphically stated the unwholesome reasons which make the opaque system work. It is the time to realize that "Sunshine is the strongest antiseptic."

IV

SOME SUGGESTIONS FOR CONSIDERATION

(a) **U.N. Multilateral Convention on Tax Treaties:**

Long back, before he became the Judge of the International Court of Justice, Dr. Nagendra Singh had told me to take up as the subject of my doctoral research "the feasibility of a multinational convention for the avoidance of double taxation". I too felt the need for such a convention in our globalised economy on the model of the conventions on the Law of the Seas. It would be good to substitute the bilateral regime of tax treaties by a comprehensive multilateral treaty regime articulating the appropriate governing norms in conformity with international law, and also without transgressing the constitutional restraints on the treaty-making power of the Executive which cannot go counter to our Constitution even at the international plane. I suggest this for my readers to think about.

(b) **The idea of constituting International Tax Authority (ITA)**

A lot of concern has been expressed to arrest and stop the massive tax evasions, the theft of economic resources, the parking of ill-gotten gains outside by crafting sinister devices through the tax havens and offshore financial centres spread over the world around. The beneficiaries of this morbid opaque system resist/evade transparency. The extent of the damage done to the nation is massive. The gruesome extent of such money, stashed elsewhere, and generated through the opaque system, is now widely known. What is needed is an effective step to stem this evil. Some steps have been taken by some assertive governments, and an articulated schedule of action is now in place after the G-20 Economic Summit recently held in London. It is obvious that the steps contemplated to be taken are neither adequate, nor fully effective. But it is good that something has been done to end this evil. What is saddening is that the Government of India maintained its silence, or at best merely lent some inaudible murmurs to the chorus of protest against such dark areas which the rogue financial system has developed.

The points, which deserve our attention most, are how to devise an effective and vigilant system to stop the abuses aforementioned. It is time to establish an International Tax Authority (ITA) with global jurisdiction. Mere agreements to exchange information are not enough unless there is a strong political will to compel the derelict jurisdictions to become transparent. How can such agreements help us to achieve our objectives, when the legal regime of several tax havens makes them impervious and unresponsive? What information the tax havens can supply when they do not believe in gathering comprehensive information about the real residence of the corporations got incorporated in such jurisdictions, and the beneficial ownership of wealth and income the corporations hold and earn? It seems the appropriate way would be to set up the International Economic Surveillance Authority and the International Tax Authority under the U.N. system.

This Authority can be set up through the provisions of an International Multilateral Tax Convention drawn up under the U.N. mandate. It can be structurally modelled on the International Seabed Authority (ISA) constituted under the United Nations Convention on the Law of the Sea. The ISA was

established 'to organize and control all mineral-related activities in the international seabed area beyond the limits of national jurisdiction' holding income thereof for promoting international welfare the details of which need not be set out here.

The ITA can be granted, through a convention, the authority to levy and collect the following taxes:

(*i*) Levy of tax, as once suggested by James Tobin in 1970s, on transactions in the currency market (this species of tax can be called 'transaction tax') [this will dampen exchange rate volatility, and would take care of many other pathological manifestations of the present-day financial system].

(*ii*) Levy of tax on all transnational transactions including in the ken of taxation the levy of tax on the income of non-residents, and corporations incorporated outside the territory, whether directly or through subsidiaries.

(*iii*) To exercise exclusive tax jurisdiction on the cyberspace income-generating spaces, and wealth amassing vaults.

The ITA may consist of an Assembly of all states signatories to the Convention; a Council consisting of 5 executive members, elected by the members of the Assembly to function as the apex executive agency of the ITA ; a Tribunal designed to work as a court of law whose orders can operate effectively even under the domestic jurisdictions. The ITA may be granted competence to appeal to the International Court of Justice which may be given jurisdiction on all States coming within the province of the charge of international taxation under the proposed convention. If a particular State is non-cooperative, various ameliorative or punitive measures can be suggested by the ITA to the specified UN authority/agency, for necessary actions (which may even involve a reference to the Security Council).

The earnings from international taxation can go to the Consolidated Fund of the ITA out of which resources can be used for various purposes of global welfare including these:

(*i*) to finance all international organizations including the United Nations but excluding those to be specifically excluded on policy considerations (such as the WTO or IMF) ;

(*ii*) to grant resources for international humanitarian operations, and poverty alleviations;

(*iii*) to maintain a fund to meet some unprecedented crisis caused by nature's wrath, or on account of gross institutional failures;

(*iv*) to assist through various ways in the creation of better conditions of living for the poor world over;

I may hasten to mention that the suggested Convention would not be just a new version of a double taxation avoidance convention. This should be comprehensive convention superseding all tax conventions. This would be an inevitable legal consequence if the ITA becomes integral to the U.N system. Article 103 of the Charter of the U.N. says: "In the event of a conflict between the obligations of the members of the U.N. under the present Charter and their obligations under any other international agreement, their obligations under the present Charter shall prevail". I may mention that once a Convention is operative, all the authorities under domestic jurisdictions will be bound by its decisions.

(c) **'Democratic Deficit' in framing tax treaties must be removed**

Lack of transparency delights the unscrupulous most. It manifests itself in our Treaty-making power. Our Government had written to the Secretary General of the UNO that in India the treaty-making is an executive act, which was not subject to the constitutional restrains. But, the Delhi High Court has struck a different note. It held that treaty-making powers are under the restraints of the Basic Structure doctrine of our Constitution, and also under other binding constitutional limitations. I would come to this aspect of the matter in Chapter 21 of Book III of this Memoir.

(d) **Our Government's 'knowledge deficit'**

Our Government cannot afford to suffer from 'knowledge deficit' in the field of International Law. In course of the PILs I conducted before the Delhi High Court and the Supreme Court, I was shocked by the 'knowledge deficit' that our Government displayed. I would mention the following three points:

(i) I have just told you how contrary to the terms of our Constitution, our Government wrote to the Secretary General of the UNO what is wholly wrong. It communicated the UNO[24] :

"Parliament has not made any laws so far on the subject, and, until it does so, the President's power to enter into treaties (which is after all an executive act) remains unfettered by any "internal constitutional restrictions."

I intend to examine this topic in some other book. I have referred it merely to underscore the Government's poverty of knowledge. The worst demonstration of this deficit, was the way it saddled our nation with the obligations under the WTO Treaty, and the Agreements framed under its umbrella. If you are interested to know how it happened, you may go through *The Report of the Peoples' Commission on GATT* by V.R. Krishna Iyer, O. Chinnappa Reddy, D.A. Desai and Rajinder Sachar, and my *Final Act of WTO: Abuse of Treaty Making Power*[25]

(ii) The ignorance of the government becomes a disaster for the nation. This is proved, to our embarrassment, by the decision of the House of Lords in *Government of India* v. *Taylor* (27 ITR 356 HL)]. It was an appeal by the Ministry of Finance, Government of India; and this decision is a monument of our administrative incompetence and lack of the knowledge of International Public Law. Our Government deservedly courted a judicial rebuff that the public law of the foreign States is not given effect outside their jurisdictions. Under the established principles of International Law, neither the foreign public law nor the public acts of the foreign authorities can be given effect[26] in domestic jurisdictions. This doctrine is based on the principle of territorial sovereignty which is treated sacrosanct in the present-day public international law. Only through the specific terms of treaties this rule of customary public international law can be modified.

(iii) We are now passing through a phase when great vigilance and knowledge are required as we are interacting with global experts at various fora of international litigations or negotiations. I had occasions to watch our eminent lawyers and eminent judges dealing with the issues of Public International Law. I found them all suffer from 'knowledge deficit' India cannot go ahead with this sort of 'knowledge deficit'. There was a time when Mr. M.C. Setalvad, the then Attorney General of India, was frank

> enough to tell our Government that for proper presentation of a case before the World Court, experts like Professor Guggenheim and Soskice, deserved to be engaged, because he had his limitations in the field of international law. The way our cases have been represented before the Disputes Settlement Body of the WTO, and the way International Law issues were presented before our courts in the PILs, which I had filed and conducted, make our government's 'knowledge deficit' alarmingly shocking.

I was glad that my pursuits before the Delhi High Court and the Supreme Court in conducting the PIL litigations led our government to realize that its officers, even its law officers, suffered from 'knowledge deficit' in the matters pertaining to international taxation. This realization had a positive effect. The government did a good job by setting up the Directorate of International Taxation under the Director-General of International Taxation. I hope this Directorate would not only be able to handle matters of international taxation within our domestic jurisdiction, but would also be competent to present our cases when the Direct Taxes issues come up before the foreign fora.

Wherever I could, I told the leaders of the academic world to improve the standards of the teaching of international law. There was a time when our lawyers and the judges had not much to do with the intricate issues of international public law. Most of them found its study irrelevant to their professional work. But now we live in a different world. This phase of Economic Globalisation has altered our perspective. We must develop our knowledge and skills in public international law, and the art and craft of conducting litigations at foreign fora. But we must not forget our Constitution, and the restraints to which it subjects all the organs of the State. On Sept. 18, 2010, I addressed the students and the faculty members of the National Law University at Jodhpur. I told them about the challenges we are facing at international fora, and also in our domestic courts. I requested the University to do something in the matter to improve the standards of the teaching of international law, and international litigations.

I would also suggest to the Income-tax Department to set up an integrated course for the advanced study of international public law in the spheres of international taxation, commerce, trade and services. This institute can be easily set up at the National Academy of Direct Taxes at Nagpur.

NOTES AND REFERENCES

1. "The great and chief end of men uniting into commonwealths, and putting themselves under government, is the preservation of their property.", said Locke.
2. Bertrand Russell, *History of Western Philosophy* p.581
3. H.H. Monroe, Q.C., *Intolerable Inquisition? Reflections on the Law of Tax* p. 49
4. *[1869] L.R. 4 HL 100, 122*
5. (1879) 4.A.C. 197 H.L. Quoted in H.H. Monroe, *Intolerable Iinquisition? Reflections on the Law of Tax. (It contains his 1981 Hamlyn Lecture).* p. 51
6. *(1981) 2 ALL ER 93 at 107 (H L)* Quoted in H.H. Monroe p. 49.
7. *[1984] A.C. 474*
8. *O Hood Phillips' Constitutional and Administrative Law* p. 44
9. *Mohomed v. Yeoh (1916) 43 I.A. 256, 263)*
10. Vol.28 p.402:
11. Quoted by me in *vide the* Petitioner's Counter-Affidavit filed before the Hon'ble Supreme Court p. 238
12. O.Hood Phillips' *Constitutional and Administrative Law [7th Edition Pg.45]*
13. Quoted by me in Counter-Affidavit para 129
14. (a) US legal practice.The United States Constitution provides in Article VI, cl. 2 The U.S Senate must approve a tax treaty before it is made operational.
    (b) German Legal practice
    "In Germany, a tax treaty is enacted in accordance with Art. 59 Abs. and Art 105 of the Grundgesetz (the Federal Constitution). [Klaus Vogel on Double Taxation Conventions, 3rd ed. p. 24].
    (c) Canada : A tax treaty is by enactment viz. Canada-U.S. Tax Convention Act, 1984. discussed in Crown Forest Industries v. Canada
    (d) Australia: Every tax treaty is enacted under International Tax Agreements Act 1953
    (e) U.K.: A tax treaty is enacted through an Order in Council in accordance with section 788 of the Income and Corporation Act 1988 which prescribes : "Before any Order in Council proposed to be made under this section is submitted to Her Majesty in Council, a draft of the Order shall be laid before the House of Commons, and the Order shall not be so submitted unless an Address is presented to Her Majesty by the House praying that the Order be made".
    (f) In other countries tax treaties are enacted. [Philip Baker F-1 to F-3]
    (g) Treaty practice in different countries with different constitutional provisions materially differs. Oppenhheim's International Law pp 52-86
15. *e.g.* Lord Tomlin in *Duke of Westminster v. CIR, [1936] A.C. 119, Tax Cas, 490.*
16. *e.g.* Lord Simon in *Latilla v. CIR [1943] A.C. 377, 25 Tax Cas. 107.*
17. *e.g.* Templeman L.J. *In IRC v. Gravin [1980] S.T.C. 295 and W.T. Ramsay Ltd. v. IRC, [1979] S.T.C. 582.*
18. Per Donaldson L.J. *In IRC v. Garvin [1980] STC 296 at 313.*
19. *McDowell & Co v. CTO 154 ITR, 148 SC*
20. *[1984] 1 ALL ER 530*
21. J.K. Galbraith, *Culture of Contentment (Boston);* Hayek, *The Constitution of Liberty quoted by* Peter Watson, *A Terrible Beauty* p.518
22. Ashok H. Desai and S. Murlidhar, *in Supreme but Not Infallible: Essays in the Honour of the Supreme Court. (Oxford)*
23. *Vide* Hubert Monroe, *Intolerable Inquisition? Reflections on the Law of Tax, the 1981 Hamlyn Lecture*
24. Our Government's position is clear from the U.N. Doc. ST/LEG/SER.B/3, at63-64 (Dec. 1952) Memorandum of April 19, 1951 which was made in response to a circular letter addressed by the Secretary General of the U.N. to governments in January 1951
    U.N. Doc. ST/LEG/SER.B/3, at63-64 (Dec. 1952) (Memorandum of April 19, 1951) quoted in National Treaty Law and Practice ed. Duncan B Hollis, Merritt R. Blakeslee & L. Benjamin Ederington p. 356-357 *(2005 Boston).*
25. First edition and reprints 2006 Published by Centre for Study of Gobal Trade System and Development, New Delhi http://shivakantjha.org/openfile.php?filename = books finalact_wto.htm
26. *Att.-Gen. For the U. K. v. Heinemann Publishers Australia Pty Ltd. (1988) 62, Australian Law Journal Reports 344; Government of India v. Taylor (27 ITR 356 HL).*