Beating the Black Money Crackdown

Round tripping, changing shell company names, becoming NRIs are favourite methods to avoid declaring the cash

The promoter of a Delhi-based, mid-sized, listed company has a Rs.700-crore problem. The cash is in various overseas accounts but the businessman has no plans of declare it before the black money deadline of September 30. Instead, he plans to invest it in the Indian capital markets by opening new intermediary or shell companies in the coming year or so.

He's not alone. Many promoters of listed companies are working overtime with chartered accountants to devise ways of utilising unaccounted funds.

These include shutting old intermediary companies, starting new ones with fresh records, transferring funds to newer safe harbours and round-tripping funds into the Indian capital markets through participatory notes and even applying for non-resident Indian (NRI) status.

“Despite government assurances, many promoters of listed firms fear that if they declare their unaccounted funds in India, it would mean that they flouted many rules,“ said the managing director of a family-owned accountancy firm advising many such promoters.

ET spoke to tax advisors and accountants in Mumbai and New Delhi advising prominent promoters. None of the “big fish“ have declared their unaccounted money to the Indian tax authorities, said one of them. Some expect the government to postpone the deadline for one more month on the last day. They didn't want to be named.

The Rs.700-crore `problem' cited above stems from the promoter's order for raw materials worth around Rs.1,000 crore from companies registered in tax havens.

“These companies were basically owned by the promoters' relatives through a complex structure,“ an advisor told ET. The real cost of the raw materials was Rs.300 crore and the rest of the amount was diverted through relatives' companies to another bank account. “For the next few months thereafter, the unaccounted Rs.700 crore was invested in the promoter's company through P-notes.“

The promoter is now shutting the intermediary companies that were used to invest and then cash out in the last few months.

“Since the intermediary companies are shut, it's next to impossible to find out who the final beneficiary of the money is,“ the accountant said.“Even if the Indian government were to find out who the investors were, they would find that there are around four layers of different companies registered in four different tax havens to mask the real identities.“

To be on the safe side, the promoter is re-investing in various companies and not just his own.

The promoter of a private equity in vested company is on tenterhooks for different reasons.“The PE firm had invested in In dia through a tax haven but the ac tual money came from the promo ter,“ said a tax advisor based in Mumbai. “The promoter first opened a couple of firms in the British Virgin Islands and then became an investor in a fund of the PE firm.“

Thereafter, the PE fund invested the money in the company at an SPV (special purpose vehicle) level. Now the promoter is planning to shut down the companies that he had set up in the British Virgin Islands.

“The issue here is when the PE firm exits the investment, how would it return the money to the promoter's new companies? He cannot even declare this investment as black money, because he doesn't have any money on hand now and tomorrow some random regulator could target him,“ the adviser added.

Some promoters are abandoning their Indian citizenship. Others have persuaded sons and daughters to become NRIs so they can manage funds stashed abroad.

“People now fear that the government may go after them after the black money deadline. And cash stashed in banks abroad is the easiest to get hold of, “said the tax ad visor. However, the Indian government may not have a jurisdiction on the accounts of NRIs. “Becoming an NRI is not the main trick, it's more like an insurance, “said the tax advisor.

In another case, the chairman of a Mumbai-headquartered listed firm routed unaccounted funds to buy equity in his own company. In the five years since, the shares have risen significantly and the stake is now valued at around Rs. 850 crore.

“The stake is officially in the name of an investment arm owned by his nephew and his family. The promoter is now worried that with the black money law kicking in, his relatives could usurp the money by threatening to expose him to the Indian tax authorities, “said a tax advisor.

In this instance, the promoter has gone to the US to cajole his relatives into selling the stake and investing it in equity and real estate there, the advisor said.

Promoters are right to feel jittery. The worry about relatives siphoning off money came true for one promoter, when his son diverted Rs.91.3 crore from his Singapore account.

(Economic Times)