THE ANATOMY OF MONEY LAUNDERING

Dr. Anuradha Girme (Assistant Professor New Law College, Bharati Vidyapeeth (Deemed to be) University

Aakanchha Ray, LL.M. (2nd Year) IVth Semester, New Law College, Bharati Vidyapeeth (Deemed to be) University, Pune

Type your text

ABSTRACT

India's promising status as a financial hub and its system of informal cross-border money flows have made the country vulnerable to money laundering. Dealing with money laundering is one of the most important tasks of the financial sector. Money laundering has always been the topic of discussion nationally and internationally. Money laundering refers to the conversion of money earned from illegal sources into legitimate sources. The origin of such income may arise from drug trafficking, corruption, embezzlement, gambling, or any other activities that put society at a loss the very moment they get underway. Money laundering typically consists of three stages: **Placement** (i.e., removing the money from any involvement in the crime directly), **Layering** (i.e., splitting the test to thwart pursuit), and **Integration** (i.e., using legitimate transactions to hide illegal money). It is cause for concern for both developed and developing countries. Several financial institutions and government bodies have implemented Anti-Money Laundering (AML) solutions to fight investment fraud, such as The Prevention of Money Laundering Act (PMLA)[i], 2002, passed by the Indian government. These implementations, directly or indirectly, aim to curb and combat money laundering activities.

This article endeavors to find out the recent incidents pertaining to money laundering and the challenges that it is posing to society. Examples would be news channels displaying how the ED (Enforcement Department) has registered cases of money laundering on politicians, celebrities, businesspersons, etc. from different states and raided many of their premises. And also, in this article, we are going to discuss the process of money laundering, and finally, we will be discussing the consequences of money laundering and counter-financing terrorism.

Keywords: Money Laundering, Terrorism, Crime, Financial, Illegal, Case, Fraud, Investigation, Trafficking

INTRODUCTION

There are crimes known to the general public that make the outlook vulnerable, and we as legal scholars are very much aware of them. There are also crimes that take place behind closed doors, and we remain oblivious to them in every way, and the repercussions of them are not apparent enough as well. A whole different stage of criminal activity involves both the aforementioned stages and going on to enlarge the loopholes in our economic and social systems. Just to get closer to the point, it would be extremely important to mention that 2-5% of the global GDP, or $800 billion. is laundered every year. Roughly estimating in currency, the figure would be approximately USD $ 2 trillion[ii]. The statistics at the national level too remain indifferent, and the number of cases registered by ED has escalated from July 2005 to November 2021, reaching 4637[iii]. To put matters in perspective, the mayhem being discussed here is referred to as "**Money Laundering"**. Money laundering has always been a topic of discussion, nationally and internationally. Money laundering is a global problem that affects all countries at different levels. Although many countries have benefitted for a long time by accepting the money from laundering while keeping the crime abroad, in the long run, money laundering causes a rise in criminal activities in the country. The reason being is that, when criminals get to know a country, they create a network and eventually locate their criminal activities there. It does not only threaten security but also compromises the stability, transparency, and efficiency of the financial system, thus undermining economic prosperity.

India's promising status as a financial hub and its system of informal cross-border money flows make the country vulnerable to money laundering. Dealing with money laundering is one of the most important tasks for the financial sector.

WHAT IS MONEY LAUNDERING?

Money laundering refers to the conversion of money earned from illegal sources into legitimate sources. The origin of such income may arise from drug trafficking, corruption, embezzlement, gambling, or any other illegal activity that puts us at risk the moment it gets under way. The term "Money Laundering" originates from the mafia group in the United States. These groups earned huge amounts of money from illegal activities like extortion, gambling, and so forth, and this money is shown as legal money.[iv] The money obtained through criminal activities is considered dirty, and the process "launders" it to make it look legitimate.[v]

The UN Vienna 1988 Convention addresses money laundering and defines it in Article 3.1 as follows:

"The conversion or transfer of property, knowing that such property is derived from any offense(s), for the purpose of concealing or disguising the illicit origin of the property or of assisting any person who engages in such offense(s) to evade the legal consequences of his actions."[vi]

In India, the term money laundering includes Hawala transactions. This type of transaction involves a third party acting as an intermediary between the two original parties to the exchange. In the early 1990s, there was a significant increase in hawala transactions. There are a lot of money laundering cases registered by the Enforcement Department on bureaucrats, politicians, celebrities, businesspersons, etc. from different states, and they raided many of their premises, converting the status of their illegal money into legal money, i.e., black money into white money.

STAGES OF MONEY LAUNDERING[vii]:

Money laundering typically includes three stages:

1. **Placement** is the initial step in money laundering, in which the process of shifting money into a legitimate source via financial institutions while at the same time concealing its source is undertaken.

2. The second stage involves **Layering** also known as structuring. It involves breaking the funds into small transactions eventually making them difficult to detect.

3. The third stage involves **Integration**, i.e., after being deposited in financial institutions, lawfully repaying the money to criminals.

GLOBAL INITIAVES TO CURVE MONEY LAUNDERING:

Money laundering is a cause for concern for developed as well as developing countries. Combat structural fraud, several financial institutions have begun implementing anti-money laundering (AML) systems. Countries are becoming more conscious of the risks associated with laundering criminal proceeds. Efforts were made to educate nations about the risks associated with the laundering of illicit wealth on a worldwide scale. The UN convention against illicit traffic in Narcotic Drugs and Psychotropic Substances, which was set up in 1988, was the first significant international initiative against the laundering of the proceeds of crime derived from such trafficking. After this, the G-7 nations set up the FATF at its fifteen economic summits held in Paris in 1989. The FATF was created to function as a protector and combat terrorist financing and money laundering. The FATF published its first report in 1990. Its recommendations are recognized as global anti-money laundering and counter-terrorist financing standards.[viii]

The Vienna Convention of **1988**[ix] lays down the basis for the global regulation of precursors. It offers thorough measures to combat drug trafficking, including prohibitions on money laundering and the diversion of chemicals used to make precursors. It allows for international collaboration through methods including the transfer of procedures, restricted delivery, and the extradition of drug traffickers.

LEGISLATIVE ACTIONS IN INDIA:

The Indian legal framework has several laws aimed at regulating and reducing the menace of money laundering. The **Indian Customs Act, 1962**[x] plays an important role in preventing money laundering by imposing stringent penalties, including imprisonment, for offences under the Customs Act such as smuggling, improper import and export, and mis-declaration of exports under **Section 11.**

The Indian Parliament has passed the **Prevention of Money Laundering Act** in **2002**[xi] along with The **Prevention of Money Laundering (Maintenance of Records) Rules, 2005**[xii]**,** which directly or indirectly aim to curb and combat money laundering activities and confiscate such properties that derives from money laundering[xiii]. Any individual found guilty under this Act shall face imprisonment for a term not less than three years, but not more than seven years, as well as fine[xiv].

The **Fugitive Economic Offenders Act** of **2018**[xv] was enacted with the intention of establishing measures to prevent economic offenders from avoiding the Indian legal system. The most recent addition is under the Finance Act of 2019, which was passed to implement the central government's financial proposals for the financial year 2019-20. The Finance Act, in its Part XIII, introduced provisions to strengthen the Prevention of Money Laundering Act, 2002.

The **Income Tax Act of 1961** is one of the laws that indirectly addresses the problem. Other laws that do so include the **Narcotic Drug and Psychotropic Substance Act of 1988**, and the **Conversion of Foreign Currency and Prevention of Smuggling Activities Act, 1974**, which are preventative detention laws.[xvi]

FEMA and **FERA** have imposed detailed restrictions on the hawala market to prevent money laundering activities and its use as a medium for financing terrorism. **FEMA**, rather than relying solely on rules and regulations for prevention, also focuses on improving surveillance and pre-preventive measures.

Specialized Authorities

There are few specialized authorities that deal with money laundering issues, like the Insurance Regulatory and Development Authority of India (IRDAI)[xvii], Reserve Bank of India (RBI), and the Securities and Exchange Board of India (SEBI)[xviii], who also prescribe guidelines for antimoney laundering standards based on the PMLA and Rules.

Since the Indian banking system can be seriously affected and damaged due to the risk of money laundering, the Indian Banks Association (IBA) has taken the lead in developing a selfregulatory code that aims to combat money laundering activities in the Indian banking system. Many of these institutions have been asked to put in place anti-money laundering (AML) policies to detect and prevent any such activity.

The Enforcement Department has been designated the authority to track cases of money laundering, which will have far more powers than what was available to ED under FERA.[xix]

ENTITIES RESISTING MONEY LAUNDERING ON GLOBAL LEVEL

1. United Nation,
2. World Bank, and
3. International Monetary Fund.

JUDICIAL APPROACHES

Everyone is rushing to make money. Individuals perform several activities to make money. Some individuals make money legally, but others engage in unlawful and immoral actions to get quick money. They employ numerous strategies, such as money laundering, to make such money legitimate. Therefore, it would be unjust not to include case studies, and it would be good to briefly highlight some examples that have occurred in India and are well known worldwide.

YES BANK CASE[xx]

Yes Bank was set up by Rana Kapoor and Ashok Kapoor in 2004. After Ashok Kapoor's death in 2008, YES Bank was under the complete ownership of Rana Kapoor. Post 2008, Yes Bank was aggressively lending, and it has accumulated stressed loans of Rs. 35,000 crores. Loans were given to financially weak companies, like the Anil Ambani Group, DHFL, Essel Group, IL & FS, and so on UBS, a major global financial services firm, indicated that stressed bank loans were rapidly growing. USB downgraded the stock to a SELL rating as the company was heading to doom. The IL&FS collapse was a big blow, but YES Bank did not admit its problems. RBI asked CEO Rana Kapoor to leave by January 31, 2019, suspecting bad loan practices. RBI appointed Ravneet Gill as CEO. Gill showed huge, stressed loans, and YES bank reported a loss in March 2019. Rana Kapoor sold his entire stake in November 2019, contrary to his statement that "Diamonds are forever". In 2020, the RBI tried its best to save the bank, but it failed in all its efforts and restructuring plans. Rana Kapoor was arrested by the ED because he was involved in money laundering. ED attached his properties, worth approximately INR 2203 crores (approx. USD 286 million), including the personal property of the Kapoor family. Rana Kapoor and his family have been placed under arrest by the ED on different occasions during the investigation. On February 2022, a special court in Mumbai under the PMLA of 2002 granted bail to Rana Kapoor, his wife, and Avantha group promoter Gautam Thapar. However, Kapoor and Thapar are unlikely to be released because they are being held for another case.

PUNJAB NATIONAL BANK FRAUD CASE[xxi]

The money laundering case that shook the country was that of Punjab National Bank. The swindle, allegedly perpetrated by diamond merchants Nirav Modi and Mehul Choksi, involved a fraud of over USD 2 billion. Unlike the other cases discussed above, this crime was committed by keeping the top management in complete darkness at a particular branch of Fort, Mumbai, with the help of around fifty employees of PNB. Employees of PNB issued fake bank guarantees (i.e., Letters of Understanding) to Nirav Modi to get foreign loans worth billions of dollars. Nirav Modi and Mehul Choksi got more than 1200 fake guarantees (Lou's) without any doubt. Indian authorities have worked tirelessly in their efforts to extradite the two businesspeople, both of whom have been declared fugitives till date. After a search of over a year, in March 2019, Nirav Modi was reportedly seen in London, and Choksi is believed to be in Cuba to avoid being extradited to India because there is no extradition agreement between India and Cuba. In June 2020, the ED brought back diamonds, pearls, and other jewelry worth INR 1135 crore (approx. USD 147 million) belonging to foreign entities owned by Nirav Modi and Mehul Choksi. The ED intended to formally confiscate the jewelry under the PMLA. Currently, Nirav Modi is in Wadsworth prison in south-west London, awaiting his extradition trial.

2G SPECTRUM CASE[xxii]

Spectrum, like any other natural resource, has been a significant resource ever since the technological advancements of the internet became known. In 2007, the then communications and IT minister of India, A. Raja, was supposed to sell the 2G spectrum at a fixed price. However, he limited the sale only to selected telecom companies, and when it came time to issue the license, A. Raja preponed the date to an impossibly limited time, due to which an illegal profit of Rs. Thirty billion was made. And investigation followed by Subramaniam Swamy revealed that the then communication and IT minister benefitted largely from what was called one of the biggest political scams of India, namely the 2G spectrum scam.

FODDER SCAM[xxiii]

In this case, former Bihar chief minister Lalu Prasad Yadav was charged with and convicted of money laundering. Back in the 1990s, when Jharkhand was still an unincorporated region of Bihar, a hefty sum of money (worth millions) was conveyed to the state authorities by the Centre government. Because of the current state of technology, the majority of work is being done on paper. From animal husbandry funds to poultry funds, everything from head to toe was managed by a group of government officials. The government officials were allegedly blamed by investigators on account of the aftermath of the Ranchi airport raid of 1993. In

March 1996, after everything had started seeming fishy from head to toe, a scam was reported, and the CBI was given the charge of handling the case. The CBI, after an in-depth investigation, made shocking revelations and reported a fodder scam involving around 9.4 billion[xxiv]rupees. The paperwork done by the government officials was a blatant nuisance, reporting that each hen on a poultry farm consumed 40kg of fodder. This was now an open case, and everyone involved, from state government officials to small-scale workers, was scrutinized and charged. With his initial conviction in 2013, RJD supremo Lalu Prasad Yadav has been condemned a total 14 years in prison in the four cases relating to the Dumka, Deoghar, and Chaibasa treasuries.

He was convicted in the second case in 2017, and in the third and fourth case in January and March 2018 respectively, and he was sentenced to 5 years in prison fined Rs. 60 lakhs in the fifth case in February 2022[xxv].

CONSEQUENCES:

Like any other criminal activity, money laundering too has its share of repercussions. The repercussions involve the damage of institutions in the financial sector. Apart from promoting crimes, it must be pretty obvious that it makes our infrastructure terribly vulnerable. As a result, the efficiency of the real sector drops horribly.

A large part of the global research focuses mainly on two major sectors of money laundering:

1. The first one being **drug trafficking**. More drugs, more crime, and more violence are obvious phenomena that may degrade the social life of any country to a significant extent.

2. The second focus being **terrorist attacks**. Although this relationship is pretty complicated, considering the constant attempts of terrorists to knock down money so as to avoid the monitoring and prevention of their attacks, it become all the more obvious.

3. There will be detrimental social and political implications if money laundering is not successfully addressed. With investments, organized crime can take over significant portions of the economy, infiltrate financial institutions, or buy off public officials and entire governments.[xxvi]

SUGGESTIONS:

- Successful conviction, along with the investigation, prosecution under the PMLA, requires a multi-pronged approach.

- Assessing creditworthiness of borrowers: The banker must inquire not only about the borrower's ability to pay but also about his willingness to do so.[xxvii] Determine depositors, do a background check on them, and report any questionable activity.

- There is a need for effective and better coordination and collaboration between various enforcement and intelligence agencies like the CBI, ED, SFIO, and other government agencies.

- Government of India has to strengthen its banking system. The middle and senior level employees of state-run banks do not make as much money as compared to private sector employees; hence, it has become difficult for public sector banks to attract dynamic and motivated talent.

- The Indian banking system should integrate its banking system with software like the SWIFT system, where bank transfer and payment information are updated, and it gives alerts in view of any irregularities.

- India must strengthen its governance system so that countries like Britain can easily rely on it and sent our criminals under the Extradition Treaty of 1992.

There are several factors that can help to reduce the risk of fraud, including a combination of effective fraud risk governance and robust fraud prevention and detection strategies, as well as coordinated and timely investigation and corrective action. There are many laws dealing with financial fraud, and many of these laws were created in response to financial fraud. Like India's corporate government norms were tightened after the Satyam scam and the Fugitive Economic Offender Act was passed after the PNB scam, in 2017 the ministry of corporate affairs enacted a law regarding layers of companies and limited the number of subsidiaries. The government of India should be prepared to deal with such financial fraud instead of waiting for such crimes.

CONCLUSION

As a conclusion, one can reasonably assume that money laundering is a worldwide issue that must be addressed globally. Money laundering cannot be handled without international collaboration. Criminals outwit law enforcement by deploying a team of specialists to hide their unlawful money and masquerade it as legitimates revenue. The possibility of a link between white-collar criminals, politicians, law enforcement, and mafias cannot be ruled out. Bankers have the most important role, and the operation cannot be carried out without their cooperation. The development of new high-tech, along with financial transactions, has increased the difficulty in detecting the flow of slush funds. Due to global nature of money laundering, collaboration between foreign law enforcement agencies is necessary to effectively investigate and prosecute those who in these sophisticated criminal schemes. Punitive measures must be implemented as well as international cooperation amongst judicial and law enforcement agencies to prevent money laundering. Last but not least, it is crucial to remember that just enacting anti-money laundering laws is insufficient, the law enforcement authorities must keep up with the constantly evolving demographics of money launderers, who are always devising new ways to avoid the reach of the law.

Endnotes:

---

[i] The Prevention of Money Laundering Act, 2002 (Act 15 of 2003).

[ii] Money Laundering, available at https://www.unodc.org/unodc/en/money-laundering/overview.html (Last visited on Dec 4th, 2022)

[iii] "Bank frauds, Ponzi, govt. funds swindling constitute half of ED's money laundering cases: data", *The Economic Times,* May 5, 2022, available at govt funds: Bank frauds, ponzi, govt funds swindling constitute half of ED's money laundering cases: Data - The Economic Times (indiatimes.com) (visited on Dec 4th, 2022)

[iv] Amrut Bhairagra, "Money Laundering in India", *Journal of Taxguru*, Published on 28th Jan 2022. Money Laundering in India (taxguru.in)

[v] James Chen, "Money Laundering: What It Is and How to Prevent It" *Journal of Investopedia*, Published on 29th June 2022. https://www.investopedia.com/terms/m/moneylaundering.asp

[vi] "Money Laundering", available at https://www.unodc.org/romena/en/money-laundering.html (Last visited on Dec 4th, 2022)

[vii] Abhimanyu Bhandari and Kartika Sharma. *A Critique of the Prevention of Money Laundering Act, 2002*,32 (LexisNexis, Haryana, 2021)

[viii] Dr M C Mehanathan. (1970). *Law on Prevention of Money Laundering in India*, 8 & 17 (LexisNexis, Haryana, 3rd edition, 2023)

[ix] Abhimanyu Bhandari and Kartika Sharma. *A Critique of the Prevention of Money Laundering Act, 2002*, 15 (LexisNexis, Haryana, 2021)

[x] The Customs Act, 1962 (Act 52 of 1962), S. 11.

[xi] The Prevention of Money Laundering Act, 2002 (Act 15 of 2003).

[xii] The Prevention of Money Laundering (Maintenance of Records) Rules, 2005.

xiii The Prevention of Money Laundering Act, 2002 (Act 15 of 2003).

xiv The Prevention of Money Laundering Act, 2002 (Act No. 15 of 2003), S. 4.

xv The Fugitive Economic Offenders Act, 2018 (Act 17 of 2018).

xvi Dr M C Mehanathan. (1970). *Law on Prevention of Money Laundering in India*, 19 (LexisNexis, Haryana, 3rd edition, 2023)

xvii The Insurance Regulatory and Development Authority Act, 1999 (Act 41 of 1999)

xviii Securities and Exchange Board of India Act, 1992 (Act 15 of 1992)

xix R.N. Chaudhary, *Banking Laws,* 11 (Central law publications, Allahabad, 4th edition, 2016)

xx "What is YES Bank Crisis", *Business Standard,* available at https://www.business-standard.com/about/whatis-yes-bank-crisis (Visited on March 1st, 2023)

xxi Dr Sushil Pandey & Mr Ved Prakash, "Case study on scam in Indian Banking Industry (Nirav Modi), Vol. 9, Issue 6 *Journal of Pramana Research*, 2019.

xxii Palvi Ravindra Kumar, "2G Spectrum Scam: Case Study*"*, *LAWGIC STRATUM* (Published on June 10th, 2021, https://www.lawgicstratum.com/post/2g-spectrum-scam-case-study (Visited on Feb 26th, 2023)

xxiii "What is fodder scam: A look at what all has happened since 1996"*, The Indian Express,* Jan 24, 2018, available at What is the fodder scam: A look at what all has happened since 1996 | What Is News, The Indian Express (visited on 1st March 2023)

xxiv "Fodder scam", available at https://en.wikipedia.org/wiki/Fodder_Scam (Visited on March 1st, 2023)

xxv "Fodder scam: Lalu prasad Yadav sentenced to five-year jail term in fifth case, fined rupees 60 lakhs"*, The Times of India,* Feb 21, 2022, available at, Lalu Prasad Yadav News: Fodder scam case; Lalu Prasad Yadav sentenced to five years jail term in fifth case, Rs 60 lakh fine | India News - Times of India (indiatimes.com) (Visited on March 1st, 2023)

[xxvi] "Consequences of Money Laundering", *Financial Crime Academy,* available at Consequences Of Money Laundering (financialcrimeacademy.org) (Last visited on March 2nd, 2023)

[xxvii] K.P.M. Sundharam & P.N. Varshney, *Banking Theory, Law, & Practice,* 16.1 (Sultan Chand & Sons, New Delhi, 19th rev. edition, 2012)