

INTERNATIONAL JOURNAL FOR LEGAL RESEARCH AND ANALYSIS



Open Access, Refereed Journal Multi-Disciplinary
Peer Reviewed

www.ijlra.com

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INTERNATIONAL JOURNAL FOR LEGAL RESEARCH & ANALYSIS
ISSN

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ANTI MONEY LAUNDERING LAWS IN INDIA

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Introduction

Money Laundering is the process whereby the proceeds of crime are transformed into ostensibly legitimate money or other assets. However, in a number of legal and regulatory systems the term money laundering has become conflated with other forms of financial crime, and sometimes used more generally to include misuse of the financial system (involving the things such as securities, digital currencies, credit cards, and traditional currency) including terrorism financing, tax evasion and evading of international sanctions. Most of anti-money laundering laws openly conflate money laundering, with terrorism financing (which is concerned with destination of funds) when regulating the financial system. Money obtained from certain crimes, such as extortion, insider trading, drug trafficking, illegal gambling and tax evasion is 'dirty'. It needs to be cleaned to appear to have derived from non-criminal activities so that banks and other financial institutions will deal with it without suspicion. Money can be laundered by many methods, which vary in complexity and sophistication.¹

Different countries may or may not treat tax evasion or payments in breach of international sanctions as money laundering. Some jurisdictions differentiate these for definition purposes, and others do not. Some jurisdictions define money laundering as obfuscating sources of money, either intentionally or by merely using financial systems or services that do not identify or track sources or destinations. Other jurisdictions define money laundering to include money from activity that would have been a crime in that jurisdiction, even if it were legal where the actual conduct occurred².

¹ What is Money Laundering?, Duhaime, Christine available at <http://www.antimoneylaunderinglaw.com/>

² The Anti-Money Laundering & Counter Terrorism Financing Act 2006 (Australia), the Anti-Money Laundering and Countering Financing of Terrorism Act 2009 (New Zealand), and the Anti-Money Laundering and Counter-Terrorist Financing (Financial Institutions) Ordinance (Cap 615) available at <https://www.comlaw.gov.au/Details/C2006A00169/>

Many regulatory and governmental authorities issue estimates each year for the amount of money laundered, either worldwide or within their national economy. In 1996, the International Monetary Fund estimated that two to five percent of the worldwide global economy involved laundered money. The Financial Action Task Force on Money Laundering (FATF), an intergovernmental body set up to combat money laundering, stated, Overall, it is absolutely impossible to produce a reliable estimate of the amount of money laundered and therefore the FATF does not publish any figures in this regard.³

When a criminal activity generates substantial profits, the individual or group involved must find a way to control the funds without attracting attention to the underlying activity or the persons involved. Criminals do this by disguising the sources, changing the form, or moving the funds to a place where they are less likely to attract attention. In response to mounting concern over money laundering, the Financial Action Task Force on money laundering (FATF) was established by the G-7 Summit in Paris in 1989 to develop a co-ordinated international response. One of the first tasks of the FATF was to develop Recommendations, 40 in all, which set out the measures national governments should take to implement effective anti-money laundering programmes.⁴

Concept of Money Laundering

The money laundering cycle can be broken down into three distinct stages; however, it is important to member that money laundering is a single process. The stages of money laundering include the:-

1. Placement Stage
2. Layering Stage
3. Integration Stage

The Placement Stage:-

This is the movement of cash from its source. On occasion the source can be easily disguised or misrepresented. This is followed by placing it into circulation through financial institutions, casinos, shops, bureau de change and other businesses, both local and abroad. The process of placement can be carried out through many processes including:

³ About the FATF, Money Laundering FAQ, available at <http://www.fatf-gafi.org/pages/faq/moneylaundering/>

⁴ *Ibid*

- Currency Smuggling– This is the physical illegal movement of currency and monetary instruments out of a country. The various methods of transport do not leave a discernible audit trail [FATF 1996-1997 Report on Money Laundering Typologies](#).
- Bank Complicity– This is when a financial institution, such as banks, is owned or controlled by unscrupulous individuals suspected of conniving with drug dealers and other organised crime groups. This makes the process easy for launderers. The complete liberalisation of the financial sector without adequate checks also provides leeway for laundering.
- Currency Exchanges– In a number of transitional economies the liberalization of foreign exchange markets provides room for currency movements and as such laundering schemes can benefit from such policies.
- Securities Brokers– Brokers can facilitate the process of money laundering through structuring large deposits of cash in a way that disguises the original source of the funds.
- Blending of Funds– The best place to hide cash is with a lot of other cash. Therefore, financial institutions may be vehicles for laundering. The alternative is to use the money from illicit activities to set up front companies. This enables the funds from illicit activities to be obscured in legal transactions.
- Asset Purchase– The purchase of assets with cash is a classic money laundering method. The major purpose is to change the form of the proceeds from conspicuous bulk cash to some equally valuable but less conspicuous form.

The Layering Stage

The purpose of this stage is to make it more difficult to detect and uncover a laundering activity.

It is meant to make the trailing of illegal proceeds difficult for the law enforcement agencies.

The known methods are :

- Cash converted into Monetary Instruments – Once the placement is successful within the financial system by way of a bank or financial institution, the proceeds can then be converted into monetary instruments. This involves the use of banker's drafts and money orders.
- Material assets bought with cash then sold – Assets that are bought through illicit funds can be resold locally or abroad and in such a case the assets become more difficult to trace and thus seize.

After placement comes the layering stage. The layering stage is the most complex and often entails the international movement of the funds. The primary purpose of this stage is to separate the illicit money from its source. This is done by the sophisticated layering of financial transactions that obscure the audit trail and sever the link with the original crime.

The Integration Stage

This is the movement of previously laundered money into the economy mainly through the banking system and thus such monies appear to be normal business earnings. This is dissimilar to layering, for in the integration process detection and identification of laundered funds is provided through informants. The known methods used are :

- Property Dealing – The sale of property to integrate laundered money back into the economy is a common practice amongst criminals. For instance, many criminal groups use shell companies to buy property; hence proceeds from the sale would be considered legitimate.
- Front Companies and False Loans – Front companies that are incorporated in countries with corporate secrecy laws, in which criminals lend themselves their own laundered proceeds in an apparently legitimate transaction.
- Foreign Bank Complicity – Money laundering using known foreign banks represents a higher order of sophistication and presents a very difficult target for law enforcement. The willing assistance of the foreign banks is frequently protected against law enforcement scrutiny. This is not only through criminals, but also by banking laws and regulations of other sovereign countries.
- False Import/Export Invoices – The use of false invoices by import/export companies has proven to be a very effective way of integrating illicit proceeds back into the economy. This involves the overvaluation of entry documents to justify the funds later deposited in domestic banks and/or the value of funds received from exports.

Origin & Background of Money Laundering

Money laundering offences have similar characteristics globally. There are two key elements to a money laundering offence:

1. The necessary act of laundering itself i.e. the provision of financial services; and a requisite degree of knowledge or suspicion (either subjective or objective) relating to the source of the funds or the conduct of a client.

2. The act of laundering is committed in circumstances where a person is engaged in an arrangement (i.e. by providing a service or product) and that arrangement involves the proceeds of crime. These arrangements include a wide variety of business relationships e.g. banking, fiduciary and investment management.

The requisite degree of knowledge or suspicion will depend upon the specific offence but will usually be present where the person providing the arrangement, service or product knows, suspects or has reasonable grounds to suspect that the property involved in the arrangement represents the proceeds of crime⁵. In some cases the offence may also be committed where a person knows or suspects that the person with whom he or she is dealing is engaged in or has benefited from criminal conduct.

Different jurisdictions define crime predicated the offence of money laundering in different ways. Generally the differences between the definitions may be summarized as follows:

Differences in the degree of severity of crime regarded as sufficient to predicate an offence of money laundering. For example in some jurisdictions it is defined as being any crime that would be punishable by one or more year imprisonment. In other jurisdictions the necessary punishment may be three or five years imprisonment;⁷ or

Differences in the requirement for the crime to be recognized both in the country where it took place and by the laws of the jurisdiction where the laundering activity takes place or simply a requirement for the conduct to be regarded as a crime in the country where the laundering activity takes place irrespective of how that conduct is treated in the country where it took place⁶.

In practice almost all serious crimes, including, drug trafficking, terrorism, fraud, robbery, prostitution, illegal gambling, arms trafficking, bribery and corruption are capable of predicated money laundering offences in most jurisdictions.

Tax evasion and other fiscal offences are treated as predicate money laundering crimes in most of the world's most effectively regulated jurisdictions⁷.

⁵ What is Money Laundering, International Compliance Association available at <http://www.int-comp.org/what-is-money-laundering/>

⁶ Public Fear of Terrorism in EU available at www.dtic.mil/cgi-bin/GetTRDoc?AD=ADA573813.pdf/

⁷ FAQ on Money Laundering, Financial Intelligence Unit- India, available at <http://fiuindia.gov.in/faq-moneylaundering.htm/>

The United Nations Office on Drugs and Crime (UNODC) conducted a study to determine the magnitude of illicit funds generated by drug trafficking and organized crimes and to investigate to what extent these funds are laundered. The report estimates that in 2009, criminal proceeds amounted to 3.6% of global GDP, with 2.7% (or USD 1.6 trillion) being laundered⁸.

This falls within the widely quoted estimate by the International Monetary Fund, who stated in 1998 that the aggregate size of money laundering in the world could be somewhere between two and five percent of the world's gross domestic product. Using 1998 statistics, these percentages would indicate that money laundering ranged between USD 590 billion and USD 1.5 trillion. At the time, the lower figure was roughly equivalent to the value of the total output of an economy the size of Spain.

However, the above estimates should be treated with caution. They are intended to give an estimate of the magnitude of money laundering. Due to the illegal nature of the transactions, precise statistics are not available and it is therefore impossible to produce a definitive estimate of the amount of money that is globally laundered every year. The FATF (Financial Action Task Force) therefore does not publish any figures in this regard⁹.

Evolutionary Trends of Money Laundering

As money laundering is a consequence of almost all profit generating crime, it can occur practically anywhere in the world. Generally, money launderers tend to seek out countries or sectors in which there is a low risk of detection due to weak or ineffective anti-money laundering programmes. Because the objective of money laundering is to get the illegal funds back to the individual who generated them, launderers usually prefer to move funds through stable financial systems. Money laundering activity may also be concentrated geographically according to the stage the laundered funds have reached. At the placement stage, for example, the funds are usually processed relatively close to the under-lying activity; often, but not in every case, in the country where the funds originate¹⁰.

Money laundering takes several different forms, although most methods can be categorized into one of a few types. These include 'bank methods, smurfing (also known as structuring),

⁸ About the FATF, Money Laundering FAQ, available at <http://www.fatf-gafi.org/pages/faq/moneylaundering/>

⁹ ACAMS, Financial Action Task Force available at <http://www.moneylaundering.com/Pages/Home.aspx/>

¹⁰ Ibid 8

currency exchanges, and double-invoicing’.

- a) **Structuring**: Often known as smurfing, this is a method of placement whereby cash is broken into smaller deposits of money, used to defeat suspicion of money laundering and to avoid anti-money laundering reporting requirements. A sub-component of this is to use smaller amounts of cash to purchase bearer instruments, such as money orders, and then ultimately deposit those, again in small amounts.
- b) **Bulk cash smuggling**: This involves physically smuggling cash to another jurisdiction and depositing it in a financial institution, such as an offshore bank, with greater bank secrecy or less rigorous money laundering enforcement¹¹.
- c) **Cash-intensive businesses**: In this method, a business typically involved in receiving cash uses its accounts to deposit both legitimate and criminally derived cash, claiming all of it as legitimate earnings. Service businesses are best suited to this method, as such businesses have no variable costs, and it is hard to detect discrepancies between revenues and costs. Examples are parking buildings, strip clubs, tanning beds, car washes and casinos.
- d) **Trade-based laundering**: This involves under- or overvaluing invoices to disguise the movement of money.
- e) **Shell companies and trusts**: Trusts and shell companies disguise the true owner of money. Trusts and corporate vehicles, depending on the jurisdiction, need not disclose their true, beneficial, owner. Sometimes referred to by the slang term rathole though that term usually refers to a person acting as the fictitious owner rather a business entity¹².
- f) **Round tripping**: Here, money is deposited in a controlled foreign operation offshore, preferably in a tax heaven where minimal records are kept, and then shipped back as an FDI, exempt from taxation. A variant on this is to transfer money to a law firm or similar organization as funds on account of fees, then to cancel the retainer and, when the money is remitted, represent the sums received from the lawyers as a legacy under a will or proceeds of litigation.

¹¹ U.S. Money Laundering Threat Assessment, Bulk Cash Smuggling available at <http://www.treasury.gov/resource-center/terrorist-illicit-finance/Documents/mlta.pdf/>,

¹² Overview (Prevention of Money Laundering), Department Of Revenue, Ministry Of Finance available at http://dor.gov.in/overview_pml/

- g) **Bank capture:** In this case, money launderers or criminals buy a controlling interest in a bank, preferably in a jurisdiction with weak money laundering controls, and then move money through the bank without scrutiny¹³.
- h) **Casinos:** In this method, an individual walks into a casino with cash and buys chips, plays for a while, and then cashes in the chips, taking payment in a check, or just getting a receipt, claiming it as gambling winnings.
- i) **Other gambling:** Money is spent on gambling, preferably on higher odds. The wins are shown if the source for money is asked for, while the losses are hidden.
- j) **Real estate:** Someone purchases real estate with illegal proceeds and then sells the property. To outsiders, the proceeds from the sale look like legitimate income. Alternatively, the price of the property is manipulated: the seller agrees to a contract that under-represents the value of the property, and receives criminal proceeds to make up the difference.
- k) **Black salaries:** A company may have unregistered employees without a written contract and pay them cash salaries. Dirty money might be used to pay them.
- l) **Tax amnesties:** Those that legalize unreported assets in tax havens and cash¹⁴
- A goal of money laundering is to be able to use the dirty money for private consumption. If unable to use it openly, the traditional way to keep the dirty money near is hiding it as cash at home or other places. A more modern method is a credit card connected to a tax haven bank.

Anti-Money Laundering Laws in India-PMLA

The Prevention of Money Laundering Act (PMLA), 2002 was enacted in January, 2003. The Act along with the Rules framed thereunder have come into force with effect from 1st July, 2005. Sec. 3 of PMLA defines offence of money laundering as whosoever directly or indirectly attempts to indulge or knowingly assists or knowingly is a party or is actually involved in any process or activity connected with the proceeds of crime and projecting it as untainted property shall be guilty of offence of money-laundering. It prescribes obligation of banking companies, financial institutions and intermediaries for verification and maintenance of records of the identity of all its clients and also of all transactions and for furnishing information of such transactions in prescribed form to the Financial Intelligence Unit-India (FIU-IND). It

¹³ Drug Trafficking Act, 1994 available at <http://www.legislation.gov.uk/ukpga/1994/37/contents/>

¹⁴ Tax amnesties turn HMRC into 'biggest money-laundering operation in history, Ian Cowie available at <http://blogs.telegraph.co.uk/finance/>

empowers the Director of FIU-IND to impose fine on banking company, financial institution or intermediary if they or any of its officers fails to comply with the provisions of the Act as indicated above and as stated in the facts and the statements as specified herein¹⁵.

PMLA empowers certain officers of the Directorate of Enforcement to carry out investigations in cases involving offence of money laundering and also to attach the property involved in money laundering. PMLA envisages setting up of an Adjudicating Authority to exercise jurisdiction, power and authority conferred by it essentially to confirm attachment or order confiscation of attached properties. It also envisages setting up of an Appellate Tribunal to hear appeals against the order of the Adjudicating Authority and the authorities like Director FIU-IND.

PMLA envisages designation of one or more courts of sessions as Special Court or Special Courts to try the offences punishable under PMLA and offences with which the accused may, under the Code of Criminal Procedure 1973, be charged at the same trial. PMLA allows Central Government to enter into an agreement with Government of any country outside India for enforcing the provisions of the PMLA, exchange of information for the prevention of any offence under PMLA or under the corresponding law in force in that country or investigation of cases relating to any offence under PMLA¹⁶.

Recent developments and changes in PMLA

The PMLA (Amendment) Act, 2012 has enlarged the definition of money laundering by including activities such as concealment, acquisition, possession and use of proceeds of crime as criminal activities. 'Criminal intent is the main ingredient of any offence' under money laundering.

The chances of harassment would still have been negligible had the government not proposed to change yet another provision of the same Act. Till last month, money-laundering crimes with the exception of serious ones like terrorism were taken up only when the money involved was Rs. 30 lakh or above. And that's why there have been only 165-odd cases of money laundering so far.

¹⁵ Ibid 13

¹⁶ Prevention of Money-Laundering Act, 2002, Press Information Bureau, Govt. of India available at <http://pib.nic.in/newsite/erelease.aspx?relid=9941/>

But the amended version of the Act has removed the threshold. That means all money-laundering offences, big or small, will now be taken up for investigation. If someone makes a small profit by violating Sebi Act or Environment Protection Act or even Air (Prevention and Control of Pollution) Act, the offender will be booked for money laundering. Till last month, laundering money by violating 24 such acts was considered a crime under PMLA only when the proceeds of crime used to be Rs 30 lakh and more.

The PMLA was enacted in 2002, but was amended thrice, first in 2005, then in 2009 and then 2012. The 2012 version of the amendment received president's assent on January 3, 2013, and the law became operational from February 15, when the finance ministry notified it.

The government's argument is that it had to amend the existing law once more as India became a member of the Financial Action Task Force (FATF) in October 2010. Headquartered in Paris, the FATF is an inter-governmental body that promotes policies to combat money laundering and terrorist financing. And it was the FATF that pointed out a few deficiencies in India's anti-money-laundering legislation.

Conclusion

Every year, huge amounts of funds are generated from illegal activities such as drug trafficking, tax evasion, people smuggling, theft, arms trafficking and corrupt practices. These funds are mostly in the form of cash. The criminals who generate these funds need to bring them into the legitimate financial system without raising suspicion. The conversion of cash into other forms makes it more useable. It also puts a distance between the criminal activities and the funds. The criminals who generate these funds need to bring them into the legitimate financial system without raising suspicion. The conversion of cash into other forms makes it more useable. It also puts a distance between the criminal activities and the funds. 'Money laundering' is the name given to the process by which illegally obtained funds are given the appearance of having been legitimately obtained.

The goal of a large number of criminal acts is to generate a profit for the individual or group that carries out the act. Money laundering is the processing of these criminal proceeds to disguise their illegal origin. This process is of critical importance, as it enables the criminal to enjoy these profits without jeopardising their source.

Illegal arms sales, smuggling, and the activities of organised crime, including for example drug trafficking and prostitution rings, can generate huge amounts of proceeds. Embezzlement, insider trading, bribery and computer fraud schemes can also produce large profits and create the incentive to ‘legitimise’ the ill-gotten gains through money laundering.

When a criminal activity generates substantial profits, the individual or group involved must find a way to control the funds without attracting attention to the underlying activity or the persons involved. Criminals do this by disguising the sources, changing the form, or moving the funds to a place where they are less likely to attract attention.

