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## **“IMPACT OF FINANCIAL CRIMES ON THE ECONOMY WITH INSTANCE OF PREVENTIVE ACTS”**

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### **ABSTRACT**

Financial crimes have a huge and negative impact on the Indian economy, creating an imminent threat to its growth and stability. Money laundering, tax evasion, fraud, and corruption are all examples of crimes that weaken the financial system and hinder sustainable growth. The consequences for the economy are far-reaching, affecting both the public and private sectors, and can be seen in a variety of ways. Financial crimes eliminate essential resources away from productive industries, decreasing the available capital for investment and employment growth. Furthermore, they undermine public trust in financial institutions, forcing consumers to avoid investing and saving, restricting growth in the economy. These crimes also hinder fair competition by giving those prepared to engage in criminal practices an unfair edge, hindering the development of equal opportunities for business organisations. Furthermore, financial crimes frequently result in tax revenue losses, putting additional strain on government resources and harming public welfare programmes. To address these concerns, India has put in place several preventive measures, legislation, and processes designed to deter financial crime and promote financial integrity. The PMLA and the Benami Transactions (Prohibition) Act are important legal provisions aimed at combatting money laundering and benami transactions, respectively.

***KEYWORDS – FINANCIAL CRIMES, ECONOMIC SUSTAINABILITY, FINANCIAL SYSTEM, FAIR COMPETITION, LEGAL PROVISIONS***

### **INTRODUCTION: MEANING AND FACETS**

A broad word used to define criminal behaviours involving money or other financial resources is "financial crime." It refers to any unlawful conduct that makes use of financial products, institutions, or systems for fraudulent ends, frequently with the intention of making money for

the offenders. Financial crimes are White- Collar crimes and these crimes are often committed by individuals or groups seeking to profit from illegal activities, such as drug trafficking, human trafficking, or terrorism. Financial crimes can have serious consequences for individuals and society as a whole, including economic instability, loss of public trust in financial institutions, and erosion of the rule of law. Financial crime is a complicated and constantly changing issue that needs to be addressed from various angles. Financial institutions, regulatory organisations, and law enforcement agencies all have a crucial role to play in identifying and stopping financial crimes. Increasing cross-border collaboration, strengthening anti-money laundering regulations, and utilising technology and data analytics to spot suspect activity are all effective ways to tackle financial crime.

Financial crime is a well-known and widespread problem that impacts brand value and reputation, goodwill, and revenue of many organizations. In addition to the risk of losses from financial crime itself, companies also face spiralling costs in related areas. Compliance with increasing regulation, ongoing crime detection efforts, internal investigations of potential wrongdoing, external enforcement actions and any associated fines and penalties, class action lawsuits, and other litigation are among the factors driving up both the costs and risks associated with financial crime. Globally there are two types of crimes prominently observe in the financial sector. First are the crimes which causes financial damage to a party involved in the transaction. This includes Fraud, Theft, or Corruption. Whereas, the Second type includes protecting the financial gains derived from causing damage to another party. This involves Money Laundering.

In India these white-collar crimes affect the economy in a negative way and so to combat these financial crimes government of India have enacted several economic laws such as –

- **Prevention of Corruption Act, 1988**
- **Prevention of Money Laundering Act, 2002**
- **The Benami Transaction (Prohibition) Amendment Act, 2016**
  
- There are other provisions as well which have the regulations to penalise the financial crimes which shall be discussed further in this paper.

## **TYPES OF FINANCIAL CRIMES**

Financial crimes can be considered as a tiny part of White-Collar crimes because White collar crimes are a much broader category than financial crimes. This category can include organized crime, which cannot really be considered a financial crime. White-Collar crimes have a large socio-economic affect on an individual person and on economic fabric of a country as well.

White-Collar Crime is a nonviolent crime that is frequently characterised by deception in orderto obtain losing money or property or to gain a competitive advantage for oneself or a company. This type of crimes lacks mens-rea in them. A crime committed by a person of high social standing while working was first referred to as “white-collar crime” by sociologist Edwin Sutherland in 1949. This categorization is especially accurate when the person accused of illegal activity are professionals in business, finance, or government. Nevertheless, this paper discusses contents related to financial crimes thus, some of the prominent types of financial crimes which affect economy of a country and socially implicit are-

- **CORRUPTION AND BRIBERY**
- **MONEY LAUNDERING**
- **INSIDER TRADING**
- **TAX EVASION**
- **BENAMI PROPERTY TRANSACTIONS**

This paper shall discuss these financial crimes with a broader approach along with their negative effects on the economy and further some of the preventive acts which are enacted to curtail these socio-economic offences by Government of India.

## **IMPACT OF FINANCIAL CRIMES ON THE ECONOMY**

- **CORRUPTION AND BRIBERY**

Corruption and Bribery is nothing but offering, promising, giving, accepting, or soliciting an advantage as an inducement for an illegal action, unethical or breach of trust. Individuals with political influence, such as government officials may be able to use their status and influence to launder the proceeds of corrupt activities while avoiding governmental controls Evidence that

corruption hinders economic growth through a variety of ways is one of the many disagreeable features of corruption. When there is corruption, business people are frequently informed that an upfront bribe is necessary before an enterprise can start and that corrupt authorities may later demand a portion of the investment's profits. Therefore, businessmen view corruption as a form of tax that reduces their motivation to invest, corruption significantly reduces investment and slows economic growth. When it takes the form of tax evasion or claiming improper tax exemptions, corruption may bring about loss of tax revenue. The allocation of public procurement contracts through a corrupt system may lead to lower quality of infrastructure and public services.

- **MONEY LAUNDERING**

Money laundering is a technique that allows the launderer to cover up the money's illicit and criminal origin. It is the procedure used to give the money gained from crime a legal appearance. Money laundering is a sophisticated, well-organized, skilfully carried out, and heinous crime that has an impact on the nation's social, political, legal, and economic conditions. It is a crime committed against nations, economies, the rule of law, and the global economy rather than any specific person. Money laundering affects societies and economies in many of various and negative ways. It increases criminal activity by legitimising illicit gains, weakens the fabric of society by encouraging a sense of injustice, causes changes in exchange rates, threatens financial predictability, supports terrorism by providing illicit funds, discourages foreign direct investment because of perceived risk, creates economic instability and distortion, unfairly favours criminals over the legal private sector, and undermines democratic institutions by affecting political leadership. Therefore, coordinated efforts are required to combat money laundering in order to lessen these serious negative effects.

- **INSIDER TRADING**

Insider trading in the financial markets refers to trading in securities like bonds and stocks by employees of a company who have access to confidential information about the creation of a particular security before that information is made public. Insiders can take advantage of this by purchasing or selling shares before they change in value. Insider trading has existed throughout the history of financial markets, but it peaked during the formative years of the Indian stock markets. Insider trading is widespread in emerging nations, such as India.

High liquidity is essential for financial market's existence and performance, as large trades must be made at low transaction costs. Insider trading impacts the liquidity of the market, making transaction costs higher and reducing small investor's returns. Insider trading also makes it more expensive for companies to issue stocks and bonds since it has a large effect on the supply and demand of various securities. Overall, insider trading discourages small investors from participating in the financial markets and allows the elite to maintain the unequal power imbalance they have over ordinary citizens. This imbalance leads to direct impact on the economy of any country by decreased GDP and per capita income.

- **TAX EVASION**

Tax evasion is an activity that aims to hide, understate, or falsely report income to reduce your tax liability. It comes under Tax fraud which consists not paying tax, paying less than what is due, not declaring cash transactions, fabricating income, falsifying deductions without proof etc.

Tax Evasion not only deprives governments of much-needed revenue, leading to fiscal deficits, but it also perpetuates the generation of black money. This hidden, untaxed wealth often follows Gresham's law, where "bad money drives out good," resulting in a less transparent and equitable financial system. As black money circulates within the economy, it can trigger high inflation, especially evident in sectors like real estate where prices become artificially inflated. India, for instance, grapples with the issue of black money being stashed in offshore tax havens such as Swiss banks, exacerbating the problem by siphoning off funds that could otherwise be invested domestically for the nation's development. Addressing money laundering and curbing the generation of black money is crucial not only for fiscal stability but also for fostering a more equitable society and a transparent financial environment.

- **BENAMI PROPERTY TRANSACTIONS**

The definition of a benami transaction, which is widely accepted in India, is where a person purchases a property using his or her own funds but in the name of another person, or purchases property in his or her own name and then transfers it into the name of another person, without intending to benefit such other person in either case. The transaction is referred to as "benami" and the person in whose name it is carried out as "Benamidar." Benami holding is equally widespread in relation to all types of movable properties, although often being more common in

the case of immovable properties (land and buildings), since registration of the property in the name of the owner can only ensure his or her legal title. Most Benamidar are relations generally husband, wife and children. The objective is to have the benefits of bifurcation of income and wealth without properties going away from the control or area of close relations.

Benami transactions have a significant negative influence on the economy of the nation. The government loses tax revenue that could have been used for the welfare and development of the country because it fragments activities that generate revenue. Benami agreements are a significant contributor to the growth of black money, and without reducing this flow, poverty and inequality cannot be eradicated. Benami transactions, particularly in the real estate sector, have emerged as important methods for the storage and creation of black money in India, as people prefer to invest their unreported income in real estate. These transactions have raised real estate prices, limited the options available to homebuyers, and placed owning a home out of reach for many people.

## **LEGAL MECHANISMS TO PREVENT FINANCIAL CRIME IN INDIA**

- **PREVENTION OF CORRUPTION ACT, 1988**

The Prevention of Corruption Act was enacted in order to fight corruption and other malpractices in government and public sector business in India. Under PCA, 1988 the Central Government has the power to appoint judges to investigate and try those cases where the following offences have been committed

- **Offences punishable under the act**
- **A conspiracy to commit or an attempt to commit the offences specified under the act**

The following are the offences specified under the Prevention of Corruption act –

1. Taking gratification other than legal remuneration
2. Taking gratification with the purpose of influencing a public servant, through illegal and corrupt means
3. Taking gratification with the purpose of wielding personal influence with public servant

4. Act of criminal misconduct by the public servant

- **PREVENTION OF MONEY LAUNDERING ACT, 2002**

The main motive for enacting such a legislation was to combat the crime of legalising the economic gains obtained from illegal sources. This Act authorises the Indian Government and the police officials to seize any property that they have investigated to have been earned from illegal sources or by conducting any illegal activities. As the name suggests, the PML Act was enacted to intercept or obstruct the issue of money laundering. Further, the motive was to seize any property bought or obtained by carrying out the crime of money laundering and for matters related to such an act.

The basic objectives of the PMLA are:

1. Preventing money laundering.
2. Combating the channelising of money into illegal activities and economic crimes.
3. Providing for the confiscation of property derived from or involved in money laundering.
4. Providing for any other matters connected with or incidental to the act of money laundering.

- **THE BENAMI TRANSACTION (PROHIBITION) AMENDMENT ACT, 2016**

The prohibition of Benami Property Transaction Act, 2016 is an amendment of the older Benami transaction (prohibition) Act, 1988 and has come into force from 01.11.2016. It prohibits illegal benami transaction and provides imprisonment up to seven years and the fine for violation of the act, which may extend to 25% of the fair market value of the benami property. The new law provides for authorities to conduct inquiries on any benami transactions. These are initiating officer, approving authorities, administrator, and adjudicating authority. Under the new law, the appellate tribunal will hear appeals against orders passed by the adjudicating authority. Original Benami Transactions Act 1988 has been amended to make it more stringent. Directors of shell companies who hardly get the remuneration of 10,000/- per month, Doctors, Industrialists, and politicians belong to categories of benami transactors who thrive behind such type of suspicious persons.

## **SUGGESTIONS AND WAY FORWARD**

It is essential to use multiple strategies in order to reduce financial crimes in India. First and foremost, it is crucial to strengthen regulatory bodies and improve their capacity to identify and prevent financial crimes using advanced technology and analytics. Second, increasing people's financial knowledge and awareness can enable them to see and report suspicious activity. Thirdly, increasing cooperation between law enforcement agencies, financial institutions, and international organisations can enhance the overall efficiency of investigations by allowing them to share information and intelligence on suspected criminals. Lastly, deterring potential offenders can be accomplished by enforcing high penalties and guaranteeing quick and easy fair, and transparent legal processes. Combining these tactics can improve India's ability to fight financial crime.

## **CONCLUSION**

The 1992 Indian stock market scam that shook India and immediately highlighted the loopholes in the banking sector which benefited the corrupt stockholders and brought the collapse of the Indian stock market is one of the many lessons in history that we should keep revisiting. It called for fundamental restructuring and preventive reforms in the economic sector (Harshad S. Mehta & Ors vs The State of Maharashtra, 2001). Presently we have the legislation, what we lack is the proactiveness of the financial sector and the implementation of these laws. Our judicial system is burdened with thousands of cases and the delivery of justice is rather slow so people have lost faith in the legal mechanism. The evolution of technology can be used to curb financial crimes and promote safety infrastructure. Artificial Intelligence, Machine Learning, and Data analytics can be used to distinguish fraudulent transactions from real transactions. One can only hope that India considers the necessary recommendations and moves towards a robust financial system.