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Money Laundering in India with Special Reference to the Prevention of Money Laundering Act, 2002

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Abstract

The goal and objective of this article is to contemplate and examine the concept of money laundering in India and its law enforcement. There is no denying the fact that money laundering is globally rampant and it occurs in almost every nook and corner of this world; and it typically involves transferring money through several countries in order to conceal its origin. This piece of article gradually starts with an idea of money laundering along with the process as well as techniques involved in it. It further harp upon the various initiatives and measures taken by the government to prevent money laundering with special emphasis on the initiatives, particularly focusing on the Prevention of Money Laundering Act, 2002. It also discusses the status and efforts put in by the law enforcement agencies and where they specifically lack. An endeavour has been particularly made by the authors to identify the problems or the lacunae existing in the law enforcement and thus a suggestive measure has been provided in order to improve them.

Keywords: *Money laundering, criminal activity, property, legitimate*

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INTRODUCTION

Money laundering is a method through which the proceeds of a crime are converted into an apparently legitimate money or any other asset which deems to be sound as legitimate. It is a process of concealing the criminal proceeds so as to make its origin untraceable. In simple words, it can be better understood as an act of making money that comes from one source to look like it has come from another source. INTERPOL's definition of money laundering is: “any act or attempted act to conceal or disguise the identity of illegally obtained proceeds so that they appear to have originated from legitimate sources” [1]. The mischievous act of money laundering is carried with an intention to disguise money or any other assets from the State so as to avoid its loss through taxation, judgement enforcement or confiscation. The criminals thus attempt to disguise the beginning of cash got through different illicit exercises to seem as though it was acquired from legitimate sources in light of the fact that else they won't have the capacity to utilize it as it would associate them to the criminal movement and the law requirement authorities would seize it [2].

Article 1 of EC Directive defines money laundering as “The conversion of property, knowing that such property is derived from serious crime, for the purpose of concealing or disguising the illicit origin of the property or of assisting any person who is involved in committing such an offence to evade the legal consequences of his action, and the concealment or disguise of the true nature, source, location, disposition, movement, rights with respect to, or ownership of property, knowing that such property is derived from serious crime”.

The most common types of criminals who launder the money are drug traffickers, embezzlers, corrupt politicians and public officials, mobsters, terrorists and con artists. It is evident that the drug traffickers are always in serious need of good laundering systems because they deal almost exclusively in cash, which causes all these types of problems. Criminal activities such as terrorism, financial crimes, illegal arms sales, smuggling, or illicit drug trafficking generate humongous amount of money and criminal organizations always need to find a way to use these funds without awakening suspicions about their illicit origin [3].

The ultimate aim of these criminal organisations is to unleash profits for the group or for one of its individual members. When a criminal activity generates substantial profits, the individual or groups involved in such activities deviate these funds to safe heavens by concealing the sources, changing the form or moving the funds to a place where they are less likely to attract attention. The catena behind controlling the drug money trial is that profit motivates the drug sales, and because most sales are in cash, the recipient of cash has to find some way of converting these funds into utilizable financial resources that appear to have legitimate origins [4].

The main objective behind criminalising money laundering is to make maximum profit out of the crime. The rationale for the creation of the offence is that it is wrong for individuals and organisations to assist criminals to benefit from the proceeds of their criminal activity or to facilitate the commission of such crimes by providing financial services to them [5].

PROCESS OF MONEY LAUNDERING

Money laundering is a single process however, its cycle can be broken down into three distinct stages namely, placement stage, layering stage and integration stage [6].

Stages of Money Laundering

Placement Stage

It is the phase at which criminally determined assets are presented in the financial system. At this stage, the launderer embeds the "dirty" money into a true-blue money related organization frequently in the form of cash bank deposits. This is the most dangerous phase of the washing procedure since a lot of money is quite prominent, and banks are required to report high-esteem exchanges. To control the dangers, a lot of money is separated into less obvious littler wholes that are then saved straightforwardly into a ledger, or by acquiring a progression of fiscal instruments (checks, money orders, and so on) that are then gathered and stored into accounts at another account.

Layering Stage

It is the phase at which complex monetary exchanges are done keeping in mind the end goal to cover the illicit source. At this stage, the launderer participates in a progression of transformations or developments of the cash keeping in mind the end goal to inaccessible them from their source. At the end of the day, the cash is sent through different money related exchanges in order to change its shape and make it hard to take after. Layering may comprise of a few bank-to-bank exchanges, wire exchanges between various records in various names in various nations, making stores and withdrawals to constantly shift the measure of cash in the records, changing the cash, and acquiring high-esteem things, for example, houses, boats, diamonds and cars to change these types of the cash. This is the most complex advance in any laundering plan, and it is tied in with making the starting point of the cash as difficult to follow as could be allowed. In a few examples, the launderer may camouflage the exchanges as instalments for merchandise or administrations, along these lines giving them honest for legitimate appearance [7].

Integration Stage

It is the last stage at which the 'laundered' property is re-brought into the legitimate economy. At this stage, the launderer may put the assets into land, extravagance resources, or business wanders. Now, the launderer can utilize the cash without getting captured. It is extremely hard to get a launderer amid the joining stage if there is no documentation amid the past stages.

At each of the three stages of money laundering, various techniques can be utilized. Following are the various measures adopted all over the world for money laundering, even though it is not exhaustive but it encompasses some of the most widely used methods:

Techniques of Money Laundering

Structuring Deposits

This is also 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 avoid anti-money laundering reporting requirements [8, 9].

Shell Companies

These are fake companies that exist for no other reason than to launder money. They take in dirty money as "payment" for supposed goods or services but actually provide no goods or services; they simply create the appearance of legitimate transactions through fake invoices and balance sheets [10].

Third-Party Cheques

Counter cheques or banker's drafts drawn on different institutions are utilized and cleared via various third-party accounts. Third party cheques and traveller's cheques are often purchased using proceeds of crime. Since these are negotiable in many countries, the nexus with the source money is difficult to establish [11].

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 enforcement [12].

PREVENTION OF MONEY LAUNDERING: INDIAN INITIATIVES

In India, before the enactment of Prevention of Money Laundering Act, 2002 (PMLA) the major statutes that incorporated measures to address the problem of money laundering were:

- The Income Tax Act, 1961.
- The Conservation of Foreign Exchange and Prevention of Smuggling Activities Act, 1974(COFEPOSA).
- The Smugglers and Foreign Exchange Manipulators Act, 1976 (SAFEMA).
- The Narcotic Drugs and Psychotropic Substances Act, 1985 (NDPSA).
- The Benami Transactions (Prohibition) Act, 1988.
- The Prevention of Illicit Traffic in Narcotic Drugs and Psychotropic Substances Act, 1988.
- The Foreign Exchange Management Act, 2000, (FEMA).

During the second half of the 20th century, with the increasing threat of modern and sophisticated forms of transnational criminal activity, concern has arisen over the lack of effective national laws to combat organized crime and the laundering of its proceeds. India has had separate laws to deal with smuggling, narcotics, foreign trade violations, foreign exchange manipulations etc., and also special legal provisions for preventive detention and forfeiture of property etc., which were enacted over a period of time to deal with such serious crimes. However, the provisions under one of the Indian laws, namely, the Foreign Exchange Regulation Act, 1973 (FERA) were considered to be 'draconian' and it was repealed making foreign exchange violations civil offences under a new law called the Foreign Exchange Management Act (FEMA) [13].

PREVENTION OF MONEY LAUNDERING ACT, 2002

In view of an urgent need for the enactment of a comprehensive legislation for preventing money laundering and connected activities, confiscation of proceeds of crime, setting up of agencies and mechanisms for coordinating measures for combating money laundering etc., the Prevention of Money Laundering Bill 1998 was introduced in Parliament on 4th August, 1998. The Bill received the assent of the President and became Prevention of Money Laundering Act, 2002 on 17th January 2003. The Act has come into force with effect from 1st July 2005. It has been amended in 2005, 2009 and recently in 2012. The objective of the Act is to prevent money-laundering and to provide for confiscation of property derived from, or involved in, money-laundering and for matters connected therewith or incidental thereto.

Scheme of the Act

The Act consists of 10 chapters containing 75 sections and 1 schedule divided in 5 parts. Chapter I contain section 1 and 2 which deals with short title, extent and commencement and definitions. Chapter II contains section 3 and 4 which provide for offences and punishment for money laundering. Chapter III has sections 5–11 which provide for attachment of property, adjudication and confiscation. Chapter IV has sections 12–15 which deal with obligations of banking companies, financial institutions and intermediaries. Chapter V has sections 16–24 which relate to summons, searches, seizures, retention, presumptions etc. Chapter VI has sections 25–42 which deal with the establishment, composition, qualifications, powers and procedures etc. of the Appellate Tribunal. Chapter VII has sections 43–47 which deal with Special Courts and Chapter VIII has sections 48–54 which provide for various authorities under the Act their appointment, powers, jurisdiction etc. Chapter IX has sections 55–61 which deals with reciprocal arrangement for assistance in certain matters and procedure for attachment and confiscation of property. Chapter X has sections 62–75 which deals miscellaneous provisions including punishments, cognizance of offences, offences by companies etc.

Salient Features of the Act

Offence of Money Laundering and its Punishment

An offence of money laundering is said to be committed when a person in any way deals with the proceeds of crime [14]. The proceeds of the crime referred above include the normal crimes [15] and the scheduled crimes [16]. The prescribed punishment is 3–7 years rigorous imprisonment for an offence of money laundering with fine [17]. In case of an offence mentioned under Part A [18], imprisonment would extend up to 10 years [19].

Attachment, Adjudication and Confiscation

The confiscation of the property under the Act is dealt with in accordance with the chapter III of the said Act. An official not below the rank of Deputy Director can order attachment of proceeds of crime for a period of 180 days, after informing the Magistrate. Thereafter he will send a report containing material information relating to such attachment to the Adjudicating Authority [20]. Section 8 details the procedure of adjudication. After the official forwards the report to the Adjudication Authority, this Authority should send a show cause notice to concerned person(s) within 30 days. After considering the response and all related information, the Authority can finality give the order of attachment and make a confiscation order, which will thereafter be confirmed or rejected by the Special Court.

Obligations of Banking Companies, Financial Institutions and Intermediaries

The reporting entity is required to keep a record of all material information relating to money laundering and forward the same to the Director. Such information should be preserved for 5 years [21]. The functioning of the reporting entity will be supervised by the Director who can impose any monetary penalty or issue warning or order audit of accounts, if the entity violates its obligations [22]. The Central Government, after consulting the Reserve Bank of India is authorised to specify rules relating to managing information by the reporting entity [23].

Enforcement Paraphernalia

- *Adjudicating Authority:* The Act empowers the Central Government to constitute an Adjudicating Authority having a Chairman and two members and define their scope of functioning and other terms of service. The Adjudicating Authority will operate through a Single or Division bench. The Authority has been given autonomous powers to regulate its adjudicating procedure [24].
- *Administrator:* The property laundered will be taken care of i.e. managed after confiscation by an Administrator who will act in accordance with the instructions of the Central Government [25].
- *Appellate Tribunal:* All appeals from an order made by the Adjudicating Authority will lie to an Appellate Tribunal constituted by the Central Government [26]. It will consist of two members headed by a Chairman [27]. An official can resign by sending his resignation to the Central Government thereby giving a 3 months' notice. He can also be removed by an order made by the Central Government on the grounds of misbehaviour or incapacity [28].
- *Special Courts:* The Central Government, after consulting the High Court is empowered to designate Court of Sessions as Special Courts [29]. The Special courts can try all scheduled offences and that under section 4 and also offence under section 3, but after the authority requests in this behalf [30].
- *Authorities under the Act*: There shall be the following classes of authorities for the purposes of this Act, namely:

(a) Director or Additional Director or Joint Director,

(b) Deputy Director,
(c) Assistant Director, and
(d) Such other class of officers as may be appointed for the purposes of this Act [31].

Summons, Searches and Seizures etc.
The power of surveying and scrutinizing records kept at any place is conferred on the Adjudicating Authority. The Authority may ask any of its officials to carry on the search, collect all relevant information, place identification marks and thereafter send a report to it [32]. The search of a person to be conducted is allowed if it is ordered by the Central Government. The authority authorized in this behalf cannot detain a person beyond 24 h, must ensure the presence of two witnesses, prepare a list of things seized signed by the witnesses and forward the same to the Adjudicating Authority [33]. A property confiscated or frozen under this Act can be retained for 180 days. This period can be extended by the Adjudicating Authority after being satisfied of the merits of the case. The Court or the Adjudicating Authority can subsequently also order the release of such property [34]. There shall be a presumption of the ownership of property and records recovered from a person's possession [35]. The burden of proof will be on the accused to prove that he is not guilty of an offence under this Act [36]. The offences under the Act are to be cognizable and non-bailable [37].

ANTI MONEY LAUNDERING STANDARDS
RBI issued Master Circular on Know Your Customer (KYC) norms/Anti-Money Laundering (AML) standards/Combating of Financing of Terrorism (CFT)/Obligation of banks under Prevention of Money Laundering Act, 2002 and Banks were advised to follow certain customer identification procedure for opening of accounts and monitoring transactions of a suspicious nature for the purpose of reporting it to appropriate authority. These KYC guidelines have been revisited in the context of the recommendations made by the Financial Action Task Force (FATF) on Anti-Money Laundering (AML) standards and on Combating Financing of Terrorism (CFT). Banks have been advised to ensure that a proper policy framework on KYC and AML measures with the approval of the Board is formulated and put in place.

The objective of KYC norms/AML measures/CFT guidelines is to prevent banks from being used, intentionally or unintentionally, by criminal elements for money laundering or terrorist financing activities. KYC procedures also enable banks to know/understand their customers and their financial dealings better which in turn help them manage their risks prudently.

OBLIGATION OF BANKS
Banks should keep in mind that the information collected from the customer for the purpose of opening of account is to be treated as confidential and details thereof are not to be divulged for cross selling or any other like purposes. Banks should, therefore, ensure that information sought from the customer is relevant to the perceived risk, is not intrusive, and is in conformity with the guidelines issued in this regard. Any other information from the customer should be sought separately with his/her consent and after opening the account.

Banks should ensure that any remittance of funds by way of demand draft, mail/telegraphic transfer or any other mode and issue of traveller’s cheques for value of Rs. 50,000/- and above is affected by debit to the customer’s account or against cheques and not against cash payment. Banks should ensure that provisions of Foreign Contribution (Regulation) Act, 1976 as amended from time to time, wherever applicable are strictly adhered to.

KYC Policy
Banks should frame their KYC policies incorporating the following four key elements:
- Customer Acceptance Policy;
- Customer Identification Procedures;
- Monitoring of Transactions; and
- Risk Management.

For the purpose of KYC policy, a ‘Customer’ is defined as:
- A person or entity that maintains an account and/or has a business relationship with the bank;

- One on whose behalf the account is maintained (i.e. the beneficial owner);
- Beneficiaries of transactions conducted by professional intermediaries, such as stock brokers, chartered accountants, solicitors etc. as permitted under the law; and
- Any person or entity connected with a financial transaction which can pose significant reputational or other risk to the bank, say, a wire transfer or issue of a high value demand draft as a single transaction.

THE FINANCIAL INTELLIGENCE UNIT-INDIA (FIU-IND)

While the Prevention of Money Laundering Act (PMLA) 2002, forms the core framework for combating money laundering in the country, The Financial Intelligence Unit-India (FIUIND) is the nodal agency in India for managing the AML ecosystem and has significantly helped in coordinating and strengthening efforts of national and international intelligence, investigation and enforcement agencies in pursuing the global efforts against money laundering and related crimes. These are specialized government agencies created to act as an interface between financial sector and law enforcement agencies for collecting, analysing and disseminating information, particularly about suspicious financial transactions.

In terms of the PMLA Rules, banks are required to report information relating to cash and suspicious transactions and all transactions involving receipts by non-profit organizations of value more than Rs. 10 lakhs or its equivalent in foreign currency to the Director, FIUIND in respect of transactions.

It receives prescribed information from various entities in financial sector under the Prevention of Money Laundering Act 2002 (PMLA) and in appropriate cases disseminates information to relevant intelligence/law enforcement agencies which include Central Board of Direct Taxes, Central Board of Excise and Customs Enforcement Directorate, Narcotics Control Bureau, Central Bureau of Investigation, Intelligence agencies and regulators of financial sector. FIU-IND does not investigate cases [38].

CONCLUSION

Money laundering is a nefarious activity that its presence can be felt internationally. It is rampant at a humongous level, therefore, to make a huge impact, it is mandatory that all the nations should come forward and taker a plunge to enact strict and as far as possible same laws so that the money launderers will have no room for targeting any country in order to launder their proceeds of crime by way of weakness of jurisdiction or for any other matter.

The aspect related to financial confidentiality is also a prime issue in other countries. The states are not willing for compromising with this confidentiality. There is an urgent need to draw a line for demarcation between such financial confidentiality rules and these financial institutions which are becoming day by day money laundering heavens for these launderers.

Barring this, quite a handful of people are vouching for the view that money laundering seems to be a victimless crime. They are not aware of the harmful effects of such a crime. So, there is a need of hour to educate these people and also to create an awareness among them which will infuse a sense of watchfulness amongst them towards the instances of money laundering. It would also help the countries in better law enforcement as it would be subject to public examination.

Eradicating the offence of money laundering is a gradual process because the criminals who all are involved in it are always continuously and systematically vying for new ways to accomplish it and they also try to achieve their illicit motives but the law such as Prevention of Money Laundering Act, 2002 prevalent in India has combated the money laundering to quite an extent. Moreover, several nations are entering into multiple covenants and conventions in order to strengthen their measures to tackle money laundering, the money launderers are continuously targeting and exploiting those jurisdictions which are not strong enough and do not have sufficient laws to deal with the aspect of money laundering offences which makes us to vouch for the fact that it is the need of the hour for having a definite policy on anti-money laundering. The countries who all are dealing with these nefarious activities do not have any particular pattern i.e. they have distinct patterns of operation. India has time and again taken extensive measures in order to combat the issue of money laundering and Prevention of Money Laundering Act, 2002 is a perfect epitome which gives the testimony for it. It can rightly be said that the manpower has although been tripled, as there is Directorate of Enforcement which sees after all the money laundering cases and investigations related to it in our country but there is also a Financial Intelligence Unit which tracks down and assess the risk of money laundering through the agencies reporting to it and there is also a time to time upgradation of the legislative framework through the proposed changes and amendments. However, there is still a further need to increase the enforcement and to take more stringent actions against the persons violating them. The financial institutions are mandated to deploy additional levels of control in areas such as transaction monitoring, annual review, periodic upgradation of accounts etc. Moreover, cost factor also plays a very significant role in having an effective anti-money laundering regime as high costs and low budget may lead to reduced focus and thus higher risks.

Thus, to have effective anti-money laundering measures, there should be a proper coordination between the Centre and the State for bringing a stringent law. For that, the tussle between the two should be halted. The law pertaining to money laundering should not only be the responsibility of the Centre regarding the implementation, but it should also be the responsibility of the State to implement it at the State level. It is a self-explanatory fact that more decentralised the law would be the better reach it will have. Therefore, to have an effective and consolidated anti-money laundering regime, the government and its agencies has not only to think regionally, nationally and globally rather they also have to act proactively against the violators who are in direct contravention of Prevention of Money Laundering Act, 2002.

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