Money laundering: process, effects, and precautions an Indian perspective

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Abstract: Illegal way of earning money and then turning that illegal earned money into legal through the use of legal loopholes and the process that are present in the system. Such actions from several sectors in an economy some directly some indirectly. Though some sectors have been identified and worked on still a lot is to be done. In the said paper authors have tried to find the type of people and sectors which are more involved in money laundering and at what stages they work on. The authors have also tried to find the impact and effect of money laundering on the economy and have worked around finding a way to curb the same. Legal growth for the prevention of money laundering has also been tried to study and a few insights into the legal status of money laundering in the world have been discussed.

Keywords: Money laundering: The Prevention of Money Laundering Act; Economy;

I. Introduction

Money laundering could be a method wherever the income of crime are reworked into apparently legitimate cash or alternative assets. INTERPOL’s definition of money laundering is: "any act or a tried act to hide or disguise the identity of illicitly obtained income so that they seem to be originated from legitimate sources". The criminals herein attempt to disguise the origin of cash obtained through illegal activities to appear legal it was obtained from legal sources, otherwise, they're going to not be able to use it because it would connect them to the criminal activity and also the enforcement officers would seize it(David 1995). Once a criminal activity generates substantial profits, the individual or cluster concerned in such activities route the funds to safe havens by disguising the sources, dynamical the shape or moving the funds to an area wherever they're less probably to draw in attention to (Michael Evangelist 2002). The negative effects of money laundering on an economy are onerous to place into numbers. The money establishments directly, however additionally the country’s productivity in its numerous economic sectors, like the real sector, international trade sector, and capital flows, among others; indirectly. The negative economic effects of
money laundering on economic development may be qualified in terms of 3 sectors of the economy: MONEY, REAL and EXTERNAL. Economic process (internal corruption & reputational damage); reduces productivity within the economy's real sector by amusing resources and inspiring crime and corruption, that slows economic growth; distorts the economy's external sector international trade and capital flows (reputational harm & market distortion) to the impairment of long economic development. hiding activity, so implying that the simplest attainable course of action for developing countries with relevance hiding is what can be known as the fumbling policy.

“Funds of Money Laundering flows from the developed economies to the developing economies, and in simple words, it is the flow of capital investment into developing countries.”

“When it is about Money Laundering it the crime more prevalent in developed countries and not in the developing countries as the funds are of the developed countries and the crimes also take place in the developed economies, wherein the developing countries should be more aware of not wasting their resources on such crimes and these are much hard to catch.” As a result of the Anti-Money Laundering rules and regulations have discouraged the use of funds in the developing countries and thus potential investors move their money to different countries where they have Tax Havens.

Money Laundering is the illegal way by which the criminal tries to confirm that all his illegal effort gets converted in the end and pays him. It is important that the different criminals which lay the foundation of Money Laundering such as drug traffickers, terrorist organizations, blackmailers, arms traffickers, organized crime peddlers, flesh trade organizations or credit card fraudsters – who disguise the origin of the source of income to evade tax and liabilities along with. All this is done by them to safeguard the same from prosecution.

Sectors which are involved in Money Laundering:

- Drug peddlers
- Insider traders
- Corrupt public authorities
- Terrorist organizations
- Con Artists
- Embezzlers

Activities which are termed as Criminal Activities are commonly termed for Illegal Arms Sales, Illicit drug Trafficking, Terrorist activities, Smuggling, and Human Trade generate a huge amount of money and Criminal organizations try to use the funds which are used to find the legal and safe ways to convert such activities into Legal Sources of Income. (FATF-GAFI)

II. STEPS INVOLVED IN THE PROCESS OF MONEY LAUNDERING.

The process of Money Laundering can be subdivided into three parts(Syed Azhar 2006):

2.1. Placement Stage: at this stage where the money earned from Criminal Activities is reintroduced into the Financial System. At this stage, the Criminal finds ways to insert the “Illegally earned Money also referred to as Dirty Money” into a legitimate financial system may be a financial institute or a bank may be in the form of small cash deposits. The cash is broken into small parts just to avoid the eyes of the law. The other ways by which the money is fueled into the system are by the purchase of a lot of monetary instruments (Cheques, Money Orders, etc) Criminal then the said money in the said forms are deposited into different accounts at another location.

2.2 Layering Stage: at this stage, the financial transactions are rotated in such a large number of times that it becomes nearly impossible for the authorities to track and to make it legal. These transactions are in such a way that the rotation is in distant bank accounts. Transactions from several banks both intra and inter countries with different names and it is continuous deposits and withdrawals from accounts to accounts and country to country. Along with account transfers, the criminals also invest in buying high-end products such as Bungalows. The property, jewelry, Diamonds, Yachts and Luxury cars to simply convert the money earned.

2.3 Integration Stage: at this Final Stage which criminals do is that property which is acquired and directed back into the legitimate system. This is the stage, the criminal is finding different options to invest the funds into luxuries, real estate or other business opportunities through the ways of Money Laundering. The ways can be easily studied as under:

2.3.1 Structured Deposits: commonly known as Smurfing, under this method amount of cash is subdivided into smaller parts to reduce the suspicion of Money Laundering and avoid legal issues related to the same.

2.3.2 Shell Companies: These are pretended companies that exist for no different reason than to launder cash. They soak up the booty as "payment" for supposed merchandise or services however really offer no goods or services; they merely produce the looks of legitimate transactions through pretend invoices and balance sheets.

2.3.3 Third-Party Cheques: Counter cheques or banker’s drafts drawn on totally different establishments are used and cleared via varied third-party accounts. Third-party cheques and traveler's cheques are typically purchased mistreatment yield of crime. Since these are negotiable in several countries, the nexus with the supply cash is tough to determine.

2.3.4 Bulk money importation: This involves physically smuggling cash to a different jurisdiction and depositing it in a very financial organization, like Associate in Nursing offshore bank, with larger bank secrecy or less rigorous concealing social control.

III. Effect of Money laundering

Criminals are regularly looking for new ways and methods for laundering. There are several different ways to evade the legal system, who play and move around the funds from some parts of the country to country and other parts of the world say country to country keeping in mind the flexibility and loopholes in the financial system of the countries. Organized Crimes can find a way in and out effectively into financial institutes, work around large sectors of the
economy and when it comes to investment it is minimal and it is easy for the acquire through bribes to officials on high positions or simply corrupt system. It can be easily said that if Money Laundering is left unchecked it can affect the economic growth of the nation by changing the cash demand, interest rates and exchange rates due to inflation.

3.1 Increased Crime and Corruption

Money Laundering helps in making every Criminal Activity Profitable, and leading to the Terrorist Financing:

- A weak legal system
- Some financial Institutes being out of Anti Money Laundering
- Weak enforcement of AML
- Penalties are ineffective.
- A restricted range of predicate crimes for concealment.

Money laundering leads to more crime and more corruption. It also leads to a rise in bribery and more corruption.

- Staff and management of economic establishments,
- Lawyers and accountants,
- Legislatures,
- Social control agencies,
- Superordinate authorities,
- Police authorities,
- Prosecutors, and
- Courts.

3.2 ECONOMIC IMPACT

3.2.1 THE INTERNATIONAL PROSPECT:

3.2.1.1 The health of monetary establishments and therefore the political stability of states could rely on authorities to dominant the infiltration of their markets by criminals. The global organization, in their Declaration and Action, set up against concealing, created this threat clear by stating. The washing of cash derived from illicit traffic, likewise as from alternative serious crime, has become a world threat to the integrity and stability of monetary and mercantilism system (UN). The washing of cash derived from illicit traffic, likewise as from alternative serious crime, has become a world threat to the integrity and stability of monetary and mercantilism system (UN). Concealing could challenge the integrity of monetary markets. as an example, criminals are proverbial to maneuver massive sums of money, via wire transfers, suddenly and while not notification, inflicting liquidity issues and potential bank runs. the policy is compromised. thanks to the big quantity of cash laundered every year, these funds have the potential to corner markets. concealing distorts cash demand and creates volatility in international capital flows likewise as interest and exchange rates, thereby perturbing any conceive to establish useful policy. Fourth cash launderers have interest out of sight their wealth to avoid detection instead of investment their assets incomes that will profit the. Local economy. Fifth, there's a loss of state revenue. Sixth, there are risks related to government privatization. very like the launderer's ability to
buy front firms, she is additionally ready to outbid alternative for antecedently, state closely-held enterprises. there's spare proof to demonstrate concealing negatively affects money markets and helps to sustain the criminal component.

3.2.1.2 Undermining the Legitimate non-public Sector: cash launderers typically use front firms, that co-mingle the yield of illicit activity with legitimate funds, to cover the illegal gains. within u. s., for instance, gangland has used pizza parlors to mask yield from hard drug trafficking. the management principles of those criminal enterprises don't seem to be in keeping with ancient free-market principles of legitimate business, which ends in more negative economic science effects.

3.2.1.3 Loss of management of Economic Policy: Concealing can even adversely affect currencies and interest rates as launderers reinvest funds wherever their schemes are less seemingly to be detected, instead of wherever rates of come back are higher. And concealing will increase the threat of financial instability thanks to the misallocation of resources from artificial distortions in quality and goods costs. concealing and money crime could end in paradoxical changes in cash demand and redoubled volatility of international capital flows, interest, and exchange rates. The unpredictable nature of concealing, plus the attendant loss of policy management, could create sound policy tough to realize.

3.2.1.4 Economic Distortion and Instability: Cash launderers don't seem to be curious about profit generation from their investments however rather in protecting their yield. therefore they “invest” their funds in activities that don't seem to be essentially economically useful to the country wherever the funds are settled. In some countries, for instance, entire industries, like construction and hotels, are supported not as a result of actual demand, however as a result of the short-run interests of cash launderers.

3.2.1.5 Loss of Revenue: Concealing diminishes government revenue and thus indirectly harms honest taxpayers. It additionally makes the government collecting tougher. This loss of revenue typically suggests that higher tax rates than would commonly be the case if the exempt yield of crime were legitimate.

3.2.1.6 Risks to Privatization Efforts: Concealing threatens the efforts of the many states to introduce reforms into their economies through privatization. Criminal organizations have the money wherewithal to outbid legitimate purchasers for once state-owned enterprises. criminals are ready to purchase marinas, resorts, casinos, and banks to cover their illicit yield and more their criminal activities.

3.2.1.7 Name Risk: Nations cannot afford to own their reputations associated with money establishments sullied by an association with concealing, particularly in today’s international economy. concealing and money crimes like the laundering of criminal yield, widespread money fraud, trading of securities, and misapplication. The negative name that results from these activities diminishes legitimate international opportunities and property growth whereas attracting international criminal organizations with undesirable reputations and short-run goals.
3.3 SOCIAL IMPACT

There are vital social prices and risks related to concealment. concealment could be a method very important in creating crime worthy. It permits drug traffickers, smugglers, and alternative criminals to expand their operations. This drives up the price of state thanks to the necessity for multiplied enforcement and health care expenditures (for example, for treatment of drug addicts) to combat the intense consequences that result. Among its alternative negative socioeconomic effects, concealment transfers economic power from the market, government, and voters to criminals. In short, it turns the recent saw that crime doesn’t pay on its head.

3.3.1 The Effect of Money Laundering can be summarized into the following points:

- Potential injury to the name of economic establishments and market
- Weakens the “democratic institutions” of the society
- Destabilizes economy of the country inflicting monetary crisis
- Offer impetus to criminal activities
- Policy distortion happens attributable to mensuration error and misallocation of resources
- Discourages foreign investors
- Causes monetary crisis
- Encourages nonpayment culture
- Ends up in exchange and interest rates volatility
- Provides the chance to criminals to hijack the method of privatization
- Contaminates legal group action

IV. PREVENTION OF MONEY LAUNDERING – GLOBAL INITIATIVES

Several initiatives have been engaged to deal with the problem at the international level. The major international agreements addressing money laundering include the United Nations Convention against Illicit Trafficking in Drugs and Psychotropic Substances, popularly known as the Vienna Convention. (Vienna Convention)

4.1 THE VIENNA CONVENTION

It was the first major initiative in the prevention of money laundering held in December 1988. It promotes international cooperation in investigations and makes extradition between member states applicable to money laundering. (UNODC 2015)

4.2 THE COUNCIL OF EUROPE CONVENTION

This convention in 1990 establishes a common policy on money laundering. The Convention lays down the principles for international cooperation among the member states, which may also include states outside the Council of Europe.
all types of criminality, particularly serious crimes such as drug offenses, arms dealing, terrorism offenses, etc. and other offenses that generate large profits.

4.3 BASEL COMMITTEE’S STATEMENT OF PRINCIPLES
In December 1988, the Basle Committee on Banking Regulations and Supervisory Practices issued a statement of principles which aims at encouraging the banking sector to adopt a common position to ensure that banks are not used to hide or launder funds acquired through criminal activities. It seeks to deny the banking system to those involved in money laundering by the application of the four basic principles namely, identifying the customer, compliance with the laws, cooperation with Law Enforcement Agencies and adherence to the Statement.

4.4 THE FINANCIAL ACTION TASK FORCE (FATF)
The FATF has developed a series of recommendations that are recognized as the international standards for combating money laundering and the financing of terrorism.

4.5 UNITED NATIONS GLOBAL PROGRAMME AGAINST MONEY LAUNDERING (GPML): was established in 1997 to increase the effectiveness of international action against money laundering through comprehensive technical cooperation services offered to Governments.

1. Technical cooperation is the main task of the Programme. It encompasses activities of creating awareness, institution building and training.
2. The research and analysis aimed at offering States Key Information to better understand the phenomenon of money laundering and to enable the international community to devise more efficient and effective countermeasure strategies.
3. The commitment to support the establishment of financial investigation services for raising the overall effectiveness of law enforcement measures.

V. 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)
5.1 PREVENTION OF MONEY LAUNDERING ACT, 2002

Preventing money laundering and connected activities, confiscation of proceeds of crime, setting up 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 the 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.

VI. Conclusion

Financial Crimes are rising in numbers and value terms throughout the world and India is no exception to the same. Several ways and procedure are being taken into account by criminals out of which Money Laundering is the most widely used and preferred way by which criminals from both organized and unorganized sectors to convert their illegitimate money into legitimate. Through with the time governing bodies and government have pulled their sleeves to work towards irradiating Money Laundering, but still, a lot has to be done and a lot of strict and rigid rules are to be made to curb the situation. Though the process by which it is done is known still the numbers say that the criminals are ahead of what the government is doing.

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