"Tackling the Dual Threat: Money Laundering and Terrorist Financing – Legal and Policy Perspectives "

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Abstract

Techniques for concealing the proceeds of crime include moving cash across borders, buying businesses to funnel money, acquiring easily transportable valuables, using transfer pricing, and relying on "underground banks." Since the mid-1980s, governments and law enforcement agencies have established a more global, intrusive, and standardized set of measures to target criminal money flowing through the financial system. However, the impact of these measures on laundering methods, prices, or criminals' willingness to commit various crimes is largely unknown, aside from anecdotal evidence. Available data suggests that the anti-money laundering (AML) regime has had limited success in reducing crime. While it aids in investigating and prosecuting certain criminals who would otherwise avoid justice, the number is lower than anticipated by those supporting the "follow the money" approach. The regime also allows for the easier recovery of funds from major criminals and financial intermediaries, though the amount recovered is minimal compared to the income or profits from crime. While the regime targets funding for terrorism, modern terrorists require very little money for their operations, so AML measures are unlikely to cut off their funds but may provide valuable intelligence. The controls on money laundering impose significant costs on businesses and society, warranting a more thorough analysis of their positive and negative effects.

Meaning of Money Laundering

Individuals who commit serious crimes for financial gain aim not only to avoid prison but also to enjoy the profits from their illegal activities. This enjoyment often involves immediate, sometimes flashy consumption. For those who are more cautious or who make large sums, this enjoyment may take the form of saving for future financial opportunities. This group, along with transnational criminals who need to move funds before using them, and the ways in which both public and private sectors respond globally, is the main focus of this essay.

The process of turning criminal earnings into forms that allow the offender to freely spend and invest has been a concern for both criminals and the state since the early days of the American Mafia. Initially developed in the U.S. in the 1970s to prevent the use of international banks for tax evasion, money-laundering regulations became a key part of the war on drugs. Over time, these regulations expanded into a global framework addressing a broad range of crimes, from cigarette smuggling and

corruption of high-level officials to terrorist financing. However, the inclusion of tax evasion in money-laundering laws continues to be a point of divergence in both national laws and international legal cooperation.[1]

How is money laundered and where does it occur?

This can be done by breaking large sums of cash into smaller amounts, making them less noticeable, and depositing them into a bank account. Alternatively, the launderer may buy various monetary instruments like cheques or money orders, which are then collected and deposited into accounts at different locations. Once the funds are within the financial system, the second stage, known as layering, begins. During this phase, the launderer moves or converts the funds multiple times to obscure their origins. This might involve buying and selling investments, further distancing the money from its illegal source.[2]

Money laundering, being an inherent outcome of nearly all profit-driven crimes, can occur anywhere in the world. Typically, launderers seek regions where the risk of detection is low due to weak or ineffective regulations in the country of origin. During the layering phase, the launderer may opt for offshore financial centers, major regional business hubs, or global banking centers—places that offer sufficient financial or business infrastructure. At this stage, the laundered funds might only pass through various bank accounts in different locations, ensuring that their origins or final destinations remain untraceable.[3]

Money laundering, being a natural consequence of most profit-driven crimes, can happen anywhere globally. Typically, money launderers look for areas with low detection risks due to weak or ineffective anti-money laundering measures. Since the goal of money laundering is to return the illegal funds to the individual who generated them, launderers prefer to move the money through regions with stable financial systems.

The intersection : How money Laundering facilitates terrorism funding

The connection between money laundering and terrorism financing is often seen in how illicit funds are disguised to appear legitimate. This process allows terrorist organizations to move money across borders, avoid detection, and fund their operations.[4]

Terrorism is a serious crime, so those involved strive to avoid capture. By utilizing complex financial systems and money laundering techniques, they minimize the paper trail, making it harder to trace their activities. The goal is to remain undetected. Through laundering illicit funds, these organizations can obtain substantial financial support to:

- Acquire weapons, such as guns, bombs, and biological agents
- Purchase materials needed for terrorist attacks, like chemicals
- Execute attacks

[1] https://www.journals.uchicago.edu/doi/abs/10.1086/501508
[2] https://www.emerald.com/insight/content/doi/10.1108/jmlc-05-2020-0045/full/html
[3] https://journals.sagepub.com/doi/abs/10.1177/000271620258200113
[4] https://www.imf.org/en/Topics/Financial-Integrity/amlcft

- Create media and propaganda to recruit more followers
- Operate training camps for terrorists
- Purchase vehicles for transporting illegal goods, people, and for use in attacks[5]
- Participate in human trafficking
- Obtain any other resources needed to sustain their operations and organization.

Example of Money Laundering

Ahmad's case was a landmark in the UK, where the government used newly established counter-terrorism powers to freeze all his assets and resources for the first time. He is accused of laundering large sums of money, evading US sanctions, and moving millions of pounds worth of diamonds in and out of the country. Ahmad reportedly used his valuable art collection, which allegedly included an original Andy Warhol painting, and rare gems to launder money for Hezbollah.

In 2019, sanctions were imposed on Ahmad for his role in financing Hezbollah, both through money laundering and direct financial support to the group. Despite these sanctions, Ahmad and his network continued to ship high-value art and goods (estimated to be worth over $400 million) between the US and other countries. He also transferred at least $6 million of his criminal profits to Lebanon.

Hezbollah is a Lebanon-based, Iran-backed Shia Islamist military and political group.[6]

Challenges and evolving tactics

While cash remains the dominant form of illicit financial transactions, the rise of digital currencies, or cryptocurrencies, is beginning to reshape the landscape of criminal financing.

A major challenge in combating terrorism financing is the global nature of the issue, compounded by differing laws and regulations across countries and the varying protections financial institutions have in place. To effectively tackle this problem, there must be ongoing, coordinated efforts worldwide to strengthen safeguards, ensure compliance, and identify both rogue nations and individuals involved in terrorist financing.

Without global cooperation, criminals, including those funding terrorism through money laundering, will continue to exploit vulnerabilities in the financial system.[7]

Examination of Money Laundering Act with reference to terror funding

Paris, 19 September 2024 – India has made significant progress in meeting the FATF Recommendations and has taken substantial steps to combat illicit finance. However, it is crucial for the country to continue strengthening its system as its

[5] https://www.adb.org/sites/default/files/publication/27932/countering-money-laundering.pdf
[6] https://sherloc.unodc.org/cld/st/home.html
[7] https://www.fatfgafi.org/media/fatf/documents/recommendations/pdfs/FATF_Reco

economy and financial sector expand. Key areas for improvement include ensuring that money laundering and terrorist financing cases are concluded and offenders receive appropriate sanctions, as well as adopting a risk-based and educational approach with non-profit organizations.

India faces significant terrorism and terrorist financing threats, including those linked to groups like ISIL and Al Qaeda. The country emphasizes disruption and prevention and has shown success in conducting complex financial investigations. However, there is a need to focus on concluding prosecutions and ensuring terrorist financiers are convicted and appropriately sanctioned.[8]

India must also ensure that measures to prevent non-profit organizations from being used for terrorism financing are applied following a risk-based approach, including outreach to non-profits on their risks related to terrorist financing.

Despite the complexities of India's financial system, authorities work well together to address illicit financial flows, utilizing financial intelligence. India has also seen positive outcomes in international cooperation, asset recovery, and enforcing targeted financial sanctions for proliferation financing.

Government policies

Insurers have developed systems and processes to implement the various AML/CFT requirements, overseen by their boards through audit committees. Regular reviews of these systems are conducted by internal audit departments to assess their effectiveness. The Insurance Regulatory and Development Authority of India (IRDAI) monitors compliance with these guidelines through both on-site and off-site processes.

Following amendments to the PML (Maintenance of Records) Rules in 2013, IRDAI revised the 2010 AML/CFT master circular for life insurers in alignment with the changes. The updated circular was issued on September 28, 2015.

To enhance customer verification processes, the Finance Minister announced the establishment of a Central KYC Records Registry (CKYCR) in the 2012-13 Union Budget. This registry helps avoid the duplication of KYC efforts across financial institutions. As per the 2015 amendments to the PMLA, reporting entities must upload KYC records to the CKYCR within 10 days of establishing a client relationship.

IRDAI issued a circular in July 2016, advising insurers to upload KYC records of individual policyholders to the CKYCR, and later issued another circular in January 2021, instructing insurers to upload KYC records for legal entities starting April 1, 2021.

IRDAI also issued a circular in January 2019, advising insurers not to make Aadhaar mandatory for KYC purposes but allowing it as a valid document for identity and address verification, subject to conditions. In 2019, the Ministry of Law and Justice amended the law to allow insurers to use Aadhaar authentication in a limited manner, which was later extended to 29 insurers in 2020.

In addition to these measures, IRDAI issued a circular in September 2020, introducing a Video-Based Identification Process (VBIP) to simplify the KYC process using electronic platforms.

[8] https://www.justice.gov/sites/default/files/usao/legacy/2014/10/17/rico.pdf

The UAPA was strengthened in 2013 with amendments that expanded the definition of proceeds of terrorism to include property intended for use in terrorism, and broadened Section 17, which deals with the punishment for raising funds for terrorist activities, to cover funds from both legal and illegal sources raised by individuals, terrorist organizations, or groups. It also included offenses committed by companies, societies, or trusts.

In 2011, the Financial Action Task Force (FATF) team from Paris visited India to assess the country's compliance with FATF standards. Since then, India has adhered to all FATF requirements and completed its Action Plan, which was approved by the FATF during its Plenary Meeting in June 2013.[9]

Anti-Money Laundering (AML) Laws in India

In India, the primary law governing anti-money laundering efforts is the Prevention of Money Laundering Act (PMLA), enacted in 2002. This legislation establishes a comprehensive framework to prevent and combat money laundering, detailing the legal and institutional mechanisms for enforcing anti-money laundering (AML) measures. Under the PMLA, money laundering is defined as the process of acquiring, possessing, or using the proceeds of crime. The law criminalizes money laundering and imposes severe penalties, including imprisonment and fines, for those found guilty. It also provides for the seizure and confiscation of property obtained through criminal proceeds.

The PMLA mandates financial institutions to keep records of all financial transactions and report any suspicious activities to the Financial Intelligence Unit (FIU). The FIU is responsible for analyzing and sharing this information with law enforcement agencies. The Enforcement Directorate (ED) is tasked with investigating and prosecuting money laundering offenses in India.

Compliance Requirements for Financial Institutions

Under the PMLA, financial institutions are required to implement several measures to prevent money laundering, including:

- **Customer Due Diligence (CDD):** Financial institutions must verify the identity of their customers and assess the source of their funds. They must also create a risk profile for each customer, considering factors such as location, business type, and transaction history.

- **Know Your Customer (KYC):** Financial institutions must implement KYC procedures to identify and verify customers' identities, which includes gathering customer details such as their name, address, and proof of identity.

- **Enhanced Due Diligence (EDD):** For high-risk customers, financial institutions must carry out enhanced due diligence, which may involve gathering additional information, monitoring transactions, and reviewing account activity periodically.

- **Suspicious Transaction Reporting (STR):** Financial institutions are required to report suspicious transactions to the FIU. These may include transactions that do not align with a customer’s known business or source of funds, or those with no legitimate economic purpose.

[9] https://www.thehindubusinessline.com/news/sports/ipl-spot-fixing-dawood-ibrahim-sreesanth-chargesheeted/article64099462.ece

- **Record Keeping:** Financial institutions must maintain records of all cash transactions above ten lakh rupees (or its foreign currency equivalent), including transaction details, customer identity, and the source of funds.

- **Training and Awareness:** Financial institutions must provide AML training to their staff and inform customers about the risks of money laundering and the institution's efforts to prevent it.

Laws to Prevent Financial Terrorism in India

- **Prevention of Money Laundering Act (PMLA) 2002:** This act addresses the prevention, detection, and prosecution of money laundering activities, requiring financial institutions to report suspicious activities and maintain transaction records.

- **Unlawful Activities Prevention Act (UAPA) 1967:** This law empowers the government to ban organizations involved in terrorism and freeze their assets. It also prescribes harsh penalties for individuals involved in terrorist activities.

- **Foreign Exchange Management Act (FEMA) 1999:** FEMA regulates foreign exchange transactions and prohibits money laundering and the financing of terrorism through these transactions.

- **AML and CFT Guidelines:** The Reserve Bank of India has issued guidelines to banks and financial institutions to prevent money laundering and the financing of terrorism.

Case Laws :

Pankaj Bansal v. Union of India

The Enforcement Directorate (ED) must provide the accused with the grounds for their arrest in writing. This ruling was delivered by a Supreme Court bench consisting of Justices A.S. Bopanna and Sanjay Kumar, in favor of the accused who challenged their arrest following the Punjab and Haryana High Court's decision. The accused argued that they were not given a copy of the Enforcement Case Information Report (ECIR) or any written details regarding the reasons for their arrest.

The High Court had dismissed their challenge against the legality of the arrest and did not accept their plea to cancel the arrest orders, arrest memos, or the subsequent orders remanding them to ED and judicial custody.

The Supreme Court ruled that the arrest was illegal because the grounds for the arrest were not properly communicated to the accused in writing. The Court emphasized the requirements of Section 19(1) of the Prevention of Money Laundering Act (PMLA), which mandates that the ED must inform the arrested individuals of the grounds for their arrest in written form. The Court further stated that failing to adhere to these safeguards would invalidate the arrest. These safeguards include: (1) providing the accused with written grounds for the arrest, (2) non-cooperation during the investigation should not automatically be presumed as guilt, and (3) the ED must not misuse its arrest powers maliciously or with ill intent.

While the **Vijay Madanlal** case concluded that the supply of the ECIR was not mandatory if the grounds for arrest were communicated, it did not address how these grounds should be communicated. The Supreme Court clarified that informing the accused of the arrest grounds in writing is necessary to avoid disputes about the arrest's validity.

The Court also clarified that refusing to cooperate by not providing self-incriminating answers during questioning does not imply non-cooperation, especially at the summons stage. The ED should not arrest someone based solely on the belief that they must admit guilt. The Court stated that the ED's powers under Section 19(1) must align with the constitutional safeguards in Article 22, which protect the rights of the accused.

Finally, the Court criticized the ED's conduct in the case, emphasizing that the agency must act transparently, fairly, and impartially, without political bias, when making arrests.

It is important to note that these requirements were later modified in the **Ram Kishor Arora v. Directorate of Enforcement** case in 2023. In that case, a different Supreme Court bench ruled that the Pankaj Bansal case's directions should not be applied retroactively, and the ED is only required to inform the accused orally of the arrest grounds at the time of the arrest, with written notice to be provided within 24 hours.

Rana Ayyub v. Directorate of Enforcement, 2023

This case dealt with the issue of territorial jurisdiction in the trial of offences under the Prevention of Money Laundering Act (PMLA). The petitioner challenged the summons issued by the Special Court in Ghaziabad, arguing that the case should have been heard by the Special Court in Maharashtra, where the petitioner's bank account was located, as the alleged money laundering offence occurred there.

The Supreme Court, in a judgment delivered by Justices V. Ramasubramanian and J.B. Pardiwala, explained that PMLA adopts a two-pronged approach: one for addressing the proceeds of crime and another for prosecuting the individuals involved in money laundering. The Court highlighted that while a Special Court is primarily designated for trial under Section 4 of PMLA, Section 43(2) provides it with additional jurisdiction to try other related offences.

The Court also elaborated on the scope of territorial jurisdiction, stating that the location of any of the following actions—acquisition, possession, concealment, or use of proceeds of crime—could define where the offence is considered to have occurred.

Conclusion and Suggestion

Conclusion:

The Prevention of Money Laundering Act (PMLA) 2002 plays a pivotal role in addressing terrorism financing and money laundering in India. This legislation provides a comprehensive legal framework for investigating, preventing, and prosecuting offenses related to money laundering connected to terrorism. Over time, the PMLA has assisted authorities in identifying and confiscating illicit funds flowing into terrorist organizations, thereby strengthening national security.

However, the law's effectiveness has been hindered by implementation challenges, gaps in enforcement, and the dynamic nature of terrorism financing. While there has been notable progress, there is an urgent need for reforms, enhanced

international cooperation, and more efficient financial tracking to counter the increasing threat of terrorism and related financial crimes.

Recommendations:

1. **Enhance Legal and Regulatory Frameworks:**

   ○ The provisions of the PMLA should be consistently revised to stay ahead of evolving threats related to terrorism financing and money laundering. With the rise of digital currencies and online financial platforms, it has become more difficult to trace illegal financial transactions, necessitating updates to the law to address these emerging challenges.

2. **Strengthen Global Collaboration:**

   ○ Terrorism financing is often a cross-border issue, requiring coordinated efforts on an international scale. India should strengthen its collaboration with global bodies such as the Financial Action Task Force (FATF), the United Nations, and other nations to form a unified strategy in combating terrorism financing.

3. **Leverage Technology and Improve Intelligence Sharing:**

   ○ Advanced financial technologies, such as blockchain and artificial intelligence, could play a significant role in detecting and monitoring suspicious financial transactions. By investing in these technologies and improving data-sharing systems between financial institutions and law enforcement agencies, India could enhance its ability to prevent terrorism funding.

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