

**Role of Banks in Prevention of Money Laundering In India –
An Analytical Study**

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Abstract

The illicit practice of Money laundering is highly affects the country's economy and its economic reputation in the global world. In money laundering, banks become the part of it unknowingly because bank or financial institutions are the one, which transmits or regulates the flow of money. Banks or Financial institutions are the major targets for money launderers due to their services and instruments, which help to placing or integrate the crime money. The purpose of this research article is to analyze the role or functions of Banks in prevention of money laundering in India. This article will give brief on the practice of money laundering and how Banks or FI's are easily get involved in it. Initially the researcher would like to throw some light on salient features of Prevention of Money Laundering Act, 2000 for more clarity on the topic. Later, the research article would discuss the role of Banks in prevention of money laundering in details and try to cover all-important contribution in combating the problem of money laundering in a country.

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Introduction

India has been facing the problem of money laundering for a very long time and taken some preventive measures to get control over it. The money laundering is not new but to control this problem is not easy at all specially for the developing country like India. Money laundering is the process to get back illegal money or criminal money in the roll of country's economy and legalize that money.

Definition of money laundering would be "*The act of disguising the source or true nature of money obtained through illegal means*"² Money laundering is the processing of criminal proceeds to disguise its illegal origin. Terrorism, illegal arms sales, financial crimes, smuggling, and the activities of organized crime, including drug trafficking and prostitution rings, generate huge sums. Embezzlement, insider trading, bribery and computer fraud also produce large profits and create an incentive to legitimise the ill-gotten gains through money laundering. When a criminal activity generates substantial profits, the individual or group involved in such activities route the funds to safe heavens by disguising the sources, changing the form, or moving the funds to a place where they are less likely to attract attention. Most fundamentally, money laundering is inextricably linked to the underlying criminal activity that generates it. In essence, the laundering enables criminal activity to continue.³

There are three independent steps or stages in Money Laundering as shown below:

1. Placement: "Placement" refers to the physical disposal of bulk cash proceeds derived from illegal activity.

²Available on <https://legaldictionary.net/money-laundering/> last visited on 23-03-2019 at 2:03 PM

³ Economic & commercial Laws, Available at https://www.icsi.edu/media/webmodules/publications/ECL-AUGUST_2017.pdf last visited on 23-03-2019 at 2:10 PM

2. Layering: "Layering" refers to the separation of illicit proceeds from their source by creating complex layers of financial transactions. Layering conceals the audit trail and provides anonymity.
3. Integration: "Integration" refers to the reinjection of the laundered proceeds back into the economy in such a way that they re-enter the financial system as normal business funds.⁴

Global initiatives on money laundering

The money laundering is not confined to one country but it is a global menace to the world's economy. In an era of globalization with high communication & information technology where there are great opportunities for criminals to expand their operations and transactions to the whole world more sophisticatedly. So, on international level several initiatives have been taken in the interest of public and to manage the problem of money laundering, which are as follows:-

- i. The Vienna Convention

From the very start in the fight against money laundering at the international level, the United Nations has taken an active role to promote the harmonization of countermeasures and the strengthening of international cooperation. The United Nations Convention against Illicit Traffic in Narcotic Drugs and Psychotropic Substances, adopted in December 1988 in Vienna, was the first international instrument to address the issue of proceeds of crime, and to require States to establish money laundering as a criminal offence.⁵

- ii. Financial Action Task Force (FATF)

⁴Money Laundering in Banking Sector, Mrs Sandhya Singh, Available at http://www.indianmba.com/Faculty_Column/FC746/fc746.html last visited on 28-03-2019 at 2:40 PM

⁵Money Laundering and the Financing of Terrorism: The United Nations Response, Available at <https://www.imolin.org/pdf/imolin/UNres03e.pdf> Last visited on 24-03-2019 at 12:02 AM

The Financial Action Task Force (FATF) is an inter-governmental body established in 1989 by the Ministers of its Member jurisdictions. The objectives of the FATF are to set standards and promote effective implementation of legal, regulatory and operational measures for combating money laundering, terrorist financing and other related threats to the integrity of the international financial system. The FATF is therefore a “policy-making body” which works to generate the necessary political will to bring about national legislative and regulatory reforms in these areas. The FATF monitors the progress of its members in implementing necessary measures, reviews money laundering and terrorist financing techniques and counter-measures, and promotes the adoption and implementation of appropriate measures globally. In collaboration with other international stakeholders, the FATF works to identify national-level vulnerabilities with the aim of protecting the international financial system from misuse.⁶

iii. Model Legislation on money laundering and financing of terrorism

This model law on money laundering and the financing of terrorism is the outcome of a joint effort of the United Nations Office on Drugs and Crime (UNODC) and the International Monetary Fund (IMF). It contains a comprehensive set of legal measures that a domestic law should include in order to prevent, detect, and sanction effectively, money laundering and the financing of terrorism and to enable international cooperation against these crimes.⁷

Indian initiatives on money laundering

Money laundering is an international phenomenon and certain initiatives have been already taken globally though every country has its own fight with this menace. India is also suffering from money laundering for many years. There are some common causes behind a

⁶Who we are, available at <http://www.fatf-gafi.org/about/> last visited on 23-03-2019 at 11:33 PM

⁷UN, IMF Model legislation on money laundering and financing of terrorism, December 1, 2005, Available at <https://www.imf.org/external/np/leg/amlcft/eng/pdf/amlml05.pdf> last visited o 23-03-2019 at 11:58 PM

reason of India's vulnerability to money laundering are smuggling, trafficking of narcotics drugs, illegal trade especially in diamonds, illegal evasion of income tax.

There were certain statutes enacted or were there to tackle money laundering in the country such as:-

1. The Income Tax Act, 1961
2. The Conversation of Foreign Exchange and Prevention of Smuggling Activities Act, 1976
3. The Narcotics Drugs and Psychotropic Substance Act, 1985
4. The Foreign Exchange and Management Act, 2000

Due to increase in no. of money laundering related crimes in a country Indian government came up with a separate legislation for anti-money laundering called "*The Prevention of Money Laundering Act, 2000*" (Act, 2002). This act was enacted with specific objectives to combating the problem of money laundering in India such as:-

- i. To prevent money laundering
- ii. To provide for confiscation of property derived from or involved in money- laundering act
- iii. Any other matters related to money laundering or incidental there to.

Salient features of The Prevention of Money Laundering Act, 2000:-

- i. A person shall be held guilty of offence of money laundering when a person is directly or indirectly, knowingly or unknowingly is a party or actually involved in activity or process connected with proceeds of crime (any property derived or obtained, directly or indirectly, by any person as a result of criminal activity relating to a scheduled

offence or the value of any such property)⁸ and including its concealment, possession, acquisition of untainted property⁹.

- ii. The offence of money laundering is a cognizable offence within the meaning of CrPC, 1973 which means a person can be arrested without a warrant.
- iii. Adjudicating Authority shall appoint by Central Government through notification to exercise power, jurisdiction or authority conferred in the Act, 2002. Adjudicating Authorities under this act conferred same power as vested in Civil Courts under CPC, 1908 according section 11 of the Act, 2002.
- iv. The PMLA gives extremely wide powers to the authorities to attach properties suspected to be involved in Money Laundering. Section 5 of the PMLA authorises the Director or any other officer not below the rank of Deputy Director to attach property.¹⁰
- v. The Schedule Offence are those offences listed in the lists of the Act, 2002 which are divided into 3 parts i.e., Part A, Part B or Part C.
- vi. A person committed an offence of money laundering shall be punishable with rigorous imprisonment for a term shall not be less than 3 years and which shall be extended up to 7 years and also liable for fine.¹¹

Role of Banks in prevention of money laundering

The Banks, Financial institutions or intermediaries are playing an important role in anti-money laundering in India. The banks or bank like institutions are mostly targeted by money launders and they became a part of money laundering practice without any intention of

⁸Section 2(u), The Prevention of Money Laundering Act, 2002

⁹Section 3, offence of money laundering , The Prevention of Money Laundering Act, 2002

¹⁰Available at <http://www.mondaq.com/india/x/589978/Money+Laundering/All+You+Need+To+Know+About+The+Law+Relating+To+MoneyLaundering+In+India> last visited on 27-03-2019 at 12:07 PM

¹¹Section 4, The Prevention of Money Laundering Act, 2002

involving in it. Criminals needs a huge amount of cash deposits and money transfers in banks for stages of money laundering i.e., Placements, Layering, and integration/Extraction. Banks or financial institutions need to be very careful or attentive with their each customer and should monitor every cash transaction.

Provisions under the Prevention of Money Laundering Act, 2002

Chapter IV of the Act, 2002 named Obligations Of Banking Companies, Financial Institutions And Intermediaries have following provisions :-

1. Section 12- Reporting entity to maintain records
2. Section 12A- Access to information
3. Section 13- Power of Directors to impose fine
4. Section 14- No civil or criminal proceedings against reporting entity, its directors and employees in certain cases.
5. Section 15- Procedure and manner of furnishing information by reporting entities

Every banking company, financial institution and intermediary is under an obligation to maintain a record and furnish information to the Director within such time as prescribed of all transactions, the nature and value of which may be prescribed, whether such transactions comprise of a single transaction or a series of transactions integrally connected to each other and where such series of transactions take place within a month. The said records have to be maintained for a period of 10 years from the date of transactions between the clients and the banking company or financial institution or intermediary, as the case may be. Further aforesaid entities have to maintain the records of the identity of all its clients for a period of 10 years from the date of cessation of the transactions between the clients and them.¹² To exercise the powers given under the Act, 2002, Central Government in consultation with

¹²Controlling Money Laundering in India – Problems and Perspectives, Vijay Kumar Singh (Assistant Professor of Law) available at http://www.igidr.ac.in/conf/money/mfc-11/Singh_Vijay.pdf last visited on 28-03-2019 at 2:00 PM

Reserve Bank of India issues the rule i.e., The Prevention of Money-Laundering (Maintenance of Records) Rules, 2005 for a better implementation.

Know Your Customer Guidelines

Know Your Customers (KYC) guidelines were introduced by the Reserve Bank of India in 2002 which was highly required for anti- money laundering (AML) actions. RBI has issued a 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, (PMLA), 2002¹³ which is applicable on all financial institutions and all schedule commercial banks excluding RRB's.

The objective of KYC/AML/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.¹⁴

Conclusion

Banking companies and financial institutions have been playing a significant role in the prevention of money laundering practice in India. Like, banking sector is the one which has been targeted by the money launderers and Banks or Financial Institutions are they mostly needed for cash transactions or deposit huge amount of cash in different accounts to break their money into small amounts. Banks are involved in money laundering without even having any intention. Banks or FI's have the most magnificent contribution in anti-money laundering actions. In the Prevention of Money Laundering Act, 2002, Banks, FI's or Intermediaries have obligations to maintain records and make it being available to the

¹³Available at https://www.rbi.org.in/scripts/BS_ViewMasCirculardetails.aspx?Id=4354& last visited on 28-03-2019 at 2:27 PM

¹⁴Ibid

Authorities of the Act. Know Your Customer (KYC) guidelines introduced by the Reserve Bank of India is very effective in maintaining records of their customers and enable Bank to have a positive identification of them. Central Government and RBI do time to time revised the KYC guideline and rules for maintain records which are applicable to Banks or FI's. I would like to conclude with this article that Money Laundering is highly serious and global criminal activity and to reduce the risk of this crime to be more protective and attentive. It is a huge concern for Banks and they can defend themselves from money laundering by a proper implementation of legislations present there or be more dutiful towards suspicious or irregular transactions.