



## The transactions of Black Money: A serious threat to economy

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### Abstract

This paper emphasizes the concept of money laundering, smuggling and hawala.

Money Laundering - An Organized Crime: Money Laundering has a close nexus with organized crime. Money Launderers accumulate enormous profits through drug trafficking, international frauds, arms dealing etc. Cash transactions are predominantly used for Money Laundering as they facilitate the concealment of the true ownership and origin of money. It is well recognized that through the huge profits the criminals earn from drug trafficking and other illegal means, by way of money laundering could contaminate and corrupt the structure of the State at all levels, this definitely leads to corruption. The methods of money laundering and the laws on money laundering with some important cases are clearly dealt with in this paper.

**Keywords:** money laundering, smuggling and hawala, black money, economy

### Introduction

Money laundering is the process of transforming the proceeds of crime into ostensibly legitimate money or other assets. However, in a number of legal and regulatory systems the term money laundering has become conflated with other forms of financial crime, and sometimes used more generally to include misuse of the financial system (involving things such as securities, digital currencies, credit cards, and traditional currency), including terrorism financing, tax evasion and evading of international sanctions. Most anti-money laundering laws openly conflate money laundering (which is concerned with source of funds) with terrorism financing (which is concerned with destination of funds) when regulating the financial system.

Money obtained from certain crimes, such as extortion, insider trading, drug trafficking, illegal gambling and tax evasion is "dirty". It needs to be cleaned to appear to have been derived from non-criminal activities so that banks and other financial institutions will deal with it without suspicion. Money can be laundered by many methods, which vary in complexity and sophistication

Smuggling is the illegal transportation of objects or people, such as out of a building, into a prison, or across an international border, in violation of applicable laws or other regulations.

There are various motivations to smuggle. These include the participation in illegal trade, such as in the drug trade, in illegal immigration or illegal emigration, tax evasion, providing contraband to a prison inmate, or the theft of the items being smuggled. Examples of non-financial motivations include bringing banned items past a security checkpoint (such as airline security) or the removal of classified documents from a government or corporate office. Hawala or Hewala also known as hundi, is an informal value transfer system based on the performance and honour of a huge network of money brokers, primarily located in the Middle East, North Africa, the Horn of Africa, and the Indian subcontinent, operating outside of, or parallel to,

traditional banking, financial channels, and remittance systems.

### Types of Money laundering

Money laundering is commonly defined as happening in three steps: the first step involves introducing cash into the financial system by some means ("placement"); the second involves carrying out complex financial transactions to camouflage the illegal source ("layering"); and the final step entails acquiring wealth generated from the transactions of the illicit funds ("integration"). Some of these steps may be omitted, depending on the circumstances; for example, non-cash proceeds that are already in the financial system would have no need for placement.

Money laundering takes several different forms, although most methods can be categorized into one of a few types. These include "bank methods, smurfing [also known as structuring], currency exchanges, and double-invoicing".

- **Structuring:** Often 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 to avoid anti-money laundering reporting requirements. A sub-component of this is to use smaller amounts of cash to purchase bearer instruments, such as money orders, and then ultimately deposit those, again in small amounts.
- **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.
- **Cash-intensive businesses:** In this method, a business typically involved in receiving cash uses its accounts to deposit both legitimate and criminally derived cash, claiming all of it as legitimate earnings. Service businesses are best suited to this method, as such businesses have no variable costs, and it is hard to detect discrepancies between revenues and costs. Examples are

parking buildings, strip clubs, tanning beds, car washes and casinos.

- **Trade-based laundering:** This involves under- or overvaluing invoices to disguise the movement of money.
- **Shell companies and trusts:** Trusts and shell companies disguise the true owner of money. Trusts and corporate vehicles, depending on the jurisdiction, need not disclose their true, beneficial, owner. Sometimes referred to by the slang term rat hole though that term usually refers to a person acting as the fictitious owner rather a business entity
- **Round-tripping:** Here, money is deposited in a controlled foreign corporation offshore, preferably in a tax haven where minimal records are kept, and then shipped back as a foreign direct investment, exempt from taxation. A variant on this is to transfer money to a law firm or similar organization as funds on account of fees, then to cancel the retainer and, when the money is remitted, represent the sums received from the lawyers as a legacy under a will or proceeds of litigation.
- **Bank capture:** In this case, money launderers or criminals buy a controlling interest in a bank, preferably in a jurisdiction with weak money laundering controls, and then move money through the bank without scrutiny.
- **Casinos:** In this method, an individual walks into a casino with cash and buys chips, plays for a while, and then cashes in the chips, taking payment in a check, or just getting a receipt, claiming it as gambling winnings.
- **Other gambling:** Money is spent on gambling, preferably on higher odds. The wins are shown if the source for money is asked for, while the losses are hidden.
- **Real estate:** Someone purchases real estate with illegal proceeds and then sells the property. To outsiders, the proceeds from the sale look like legitimate income. Alternatively, the price of the property is manipulated: the seller agrees to a contract that underrepresents the value of the property, and receives criminal proceeds to make up the difference.
- **Black salaries:** A company may have unregistered employees without a written contract and pay them cash salaries. Dirty money might be used to pay them.
- **Tax amnesties:** For example, those that legalizes unreported assets in tax havens and cash
- A goal of money laundering is to be able to use the dirty money for private consumption. If unable to use it openly, the traditional way to keep the dirty money near is hiding it as cash at home or other places. A more modern method is a credit card connected to a tax haven bank.

### Why money laundering is an organized crime?

Money Laundering has a close nexus with organized crime. Money Launderers accumulate enormous profits through drug trafficking, international frauds, arms dealing etc. Cash transactions are predominantly used for Money Laundering as they facilitate the concealment of the true ownership and origin of money. It is well recognized that through the huge profits the criminals earn from drug trafficking and other illegal means, by way of money laundering could contaminate and corrupt the structure of the State at all levels, this definitely leads to corruption. Further, this adds

to constant pursuit of profits and the expansion into new areas of criminal activity. Through money laundering, organized crime diversifies its sources of income and enlarges its sphere of action. The social danger of money laundering consists in the consolidation of the economic power of criminal organizations, enabling them to penetrate the legitimate economy. In advanced societies, crime is increasingly economic in character. Criminal associations now tend to be organized like business enterprises and to follow the same tendencies as legitimate firms; specialization, growth, expansion in international markets and linkage with other enterprises. The holders of capital of illegal origin are prepared to bear considerable cost in order to legalize its use.

### Statutory Laws on money laundering in India

In 2002, the Parliament of India passed an act called the Prevention of Money Laundering Act, 2002. The main objectives of this act are to prevent money-laundering as well as to provide for confiscation of property either derived from or involved in, money-laundering.

Section 12 (1) describes the obligations that banks, other financial institutions, and intermediaries have to

(a) Maintain records that detail the nature and value of transactions, whether such transactions comprise a single transaction or a series of connected transactions, and where these transactions take place within a month.

(b) Furnish information on transactions referred to in clause (a) to the Director within the time prescribed, including records of the identity of all its clients.

Section 12 (2) prescribes that the records referred to in subsection (1) as mentioned above, must be maintained for ten years after the transactions finished. It is handled by the Indian Income Tax Department.

The provisions of the Act are frequently reviewed and various amendments have been passed from time to time.

The recent activity in money laundering in India is through political parties, corporate companies and the shares market. It is investigated by the Enforcement Directorate and Indian Income Tax Department. According to Government of India, out of the total tax arrears of INR2480 billion (US\$39 billion) about INR1300 billion (US\$20 billion) pertains to money laundering and securities scam cases.

Bank accountants must record all transactions over Rs. 1 million. Bank accountants must maintain these records for 10 years. Banks also must make cash transaction reports (CTRs) and suspicious transaction reports over RS. 1 million within 7 days of doubt. They must submit the report to the Enforcement Directorate and income tax department.

### Methods and ways of smuggling

In smuggling, concealment can involve concealing the smuggled goods, or go as far as hiding the whole transport. Avoiding border checks, such as by small ships, private airplanes, through overland smuggling routes, smuggling tunnels and even small submersibles. This also applies for illegally passing a border oneself, for illegal immigration or illegal emigration. In many parts of the world, particularly the Gulf of Mexico, the smuggling vessel of choice is the go-fast boat.

Submitting to border checks with the goods or people hidden in a vehicle or between (other) merchandise, or the goods hidden in luggage, in or under clothes, inside the body (see body cavity search, balloon swallower and mule),

etc. Many smugglers fly on regularly scheduled airlines. A large number of suspected smugglers are caught each year by customs worldwide. Goods and people are also smuggled across seas hidden in containers, and overland hidden in cars, trucks, and trains. A related topic is illegally passing a border oneself as a stowaway. The high level of duty levied on alcohol and tobacco in Britain has led to large-scale smuggling from France to the UK through the Channel Tunnel. The combination of acknowledged corruption at the border and high import tariffs led smugglers in the 1970s and '80s to fly electronic equipment such as stereos and televisions in cargo planes from one country to clandestine landing strips in another, thereby circumventing encounters at the frontier between countries.

For illegally passing a border oneself, another method is with a false passport (completely fake, or illegally changed, or the passport of a lookalike).

### **How Hawala Network Operates?**

In the most basic variant of the hawala system, money is transferred via a network of hawala brokers, or hawaladars. It is the transfer of money without actually moving it. In fact, a successful definition of the hawala system that is used is "money transfer without money movement".

The unique feature of the system is that no promissory instruments are exchanged between the hawala brokers; the transaction takes place entirely on the honour system. As the system does not depend on the legal enforceability of claims, it can operate even in the absence of a legal and juridical environment. Trust and extensive use of connections, such as family relations and regional affiliations, are the components that distinguish it from other remittance systems.

Informal records are produced of individual transactions, and a running tally of the amount owed by one broker to another is kept. Settlements of debts between hawala brokers can take a variety of forms (such as goods, services, properties, transfers of employees, etc.), and need not take the form of direct cash transactions.

In addition to commissions, hawala brokers often earn their profits through bypassing official exchange rates. Generally, the funds enter the system in the source country's currency and leave the system in the recipient country's currency. As settlements often take place without any foreign exchange transactions, they can be made at other than official exchange rates.

Hawala is attractive to customers because it provides a fast and convenient transfer of funds, usually with a far lower commission than that charged by banks. Its advantages are most pronounced when the receiving country applies unprofitable exchange rate regulations (as has been the case for many typical receiving countries such as Egypt) or when the banking system in the receiving country is less complex (e.g., due to differences in legal environment in places such as Afghanistan, Yemen, Somalia). Moreover, in some parts of the world it is the only option for legitimate fund transfers, and has even been used by aid organizations in areas where it is the best-functioning institution

### **Famous and well known The Jain Hawala Case in India**

The Hawala scandal or hawala scam was an Indian political scandal involving payments allegedly received by politicians through hawala brokers, the Jain brothers. It was a US\$18 million bribery scandal that implicated some of the

country's leading politicians. There were also alleged connections with payments being channeled to Hizbul Mujahideen militants in Kashmir.

### **What were the Fake measures in Jain Hawala Case?**

The famous Jain hawala case and the Indian establishment's persistent refusal to face the truth have once again come into focus with the arrest of Hurriyat leader Ali Shah Geelani. Geelani was arrested last month on charges of acting as a conduit for funding terrorism

Geelani is alleged to have got funds from the London-based Dr. Ayub Thuker. The same Dr Thuker was seen behind the hawala funds for Kashmiri terrorists that figured in the Jain hawala case in 1991. The Central Bureau of Investigation accidentally chanced upon a Byzantine nexus of politicians, bureaucrats, businessmen and film industry that sustained each other sharing slush funds coming through hawala.

Spys working on the case were led to Jain brothers — SK Jain, NK Jain and BR Jain — who passed the money on to Kashmir terrorists through the two arrested Kashmiris. However the Jain brothers were not detained for a day, nor charged under TADA (Terrorist and Disruptive Activities Act) while the Kashmiris were convicted and put behind the bars for years. This anomaly showed that the system was not even-handed. The CBI seized their diaries in which the accounts of payments were kept.

### **What happened in Jain Hawala Case <sup>[1]</sup>?**

The judge said there was no prima facie evidence against the accused which could be converted into legal evidence. The 20 accused in the hawala case have been discharged by the Delhi high court and the trial court. These include Bharatiya Janata Party president L K Advani and former Union ministers V C Shukla, Arjun Singh, Madhavrao Scindia, N D Tiwari and R K Dhawan and former Delhi chief minister Madan Lal Khurana.

Allowing the petitions by Advani and Shukla challenging the special judge's order, Justice Shamim had ruled in his 70-page judgment that the Jain diaries could not be converted into legal evidence against them.

Allowing similar petitions by the Jain brothers, S K Jain, N K Jain and B R Jain and their employee, J K Jain, the high court quashed the proceedings against them too. The said evidence is of such a nature which cannot be converted into legal evidence against the petitioners," the high court had observed.

The quashing of charges against Advani and Shukla by the high court triggered a spate of petitions with the trial court by other politicians involved in the hawala case, seeking exoneration.

On May 16 last, Judge Gupta discharged Khurana and the four Jains, stating that the Central Bureau of Investigation had failed to produce any evidence which could be converted into "legal evidence" to frame charges against the accused.

Even as the government was considering the CBI request to file a special leave petition with the Supreme Court challenging the high court order, Judge Gupta discharged Arjun Singh, Tiwari, Scindia, Dhawan and the Jains on May 28.

Citing the high court order, he said, "When the diaries, notebooks and loose sheets cannot be legal evidence in one

<sup>1</sup> Central Bureau of Investigation v. V.C. Shukla [(1998) 3 SCC 410].

case arising out of the same first information report, then certainly it cannot be legal evidence in the present cases based on the same FIR.

The Jain Hawala Case, without doubt is extra ordinary in our judicial history. It has attracted wide publicity and is responsible for exposing many scandals. Because of the above mentioned special. Features, it is cited as an example of unparalleled judicial activism. Unfortunately, such an extra ordinary case has not yielded any extra ordinary results. In spite of it, it shall be read over and over again as an example of judicial independence and impartiality.

### **Conclusion**

- Money laundering, smuggling and hawala threaten economic development.
- The international financial community should strongly support anti-laundering efforts, and cooperate to share information, and regulatory and enforcement actions.
- Developing countries should impose anti-laundering laws to improve the credibility of not only its financial sector, but its governance as well.

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