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Money-Laundering in Pakistan: Methods and means of Money Laundering and its connection with Terror Financing

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ABSTRACT

Money laundering is a global issue causing threats to the security and stability of countries around the world. There are different means and methods used for money laundering all over the world. The purpose of this study is to define money laundering with special reference to Pakistan. The study starts with the delineation of the concept "Money Laundering", its stages, methods to carry out such and its impact on national, regional and global socio-economic indicators. It discusses money laundering in Pakistan and significant channels that are deeply rooted in it. It analysis the loopholes in the previous laws, flaws in prosecuting agencies, and administrative drawbacks that permeated this issue on Pakistani soil. In the last part, this study discussed the current legal setup dealing with money laundering and finally review the legislation and agencies in Pakistan concerning Money Laundering.

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1. Introduction

The fact that people fight, struggle, plan, plot and lust for money is accepted worldwide (Madinger, 2011). This endless desire for cash has led people to commit enormous crimes all over the world, such as forgery, fraud on credit cards, evasion of taxes, terrorist financing, money laundering, fraud against the mortgage, embezzlement, bank fraud, insider trading etc (Money Laundering & Terrorist Financing – Are you aware?, n.d.). The international community (Khalil & Akhtar, 2020) is concerned about money laundering and terrorism financing. Money laundering is the practice of moving funds gained via unlawful methods (Madinger, 2011) into and out of another nation without paying the necessary taxes on the transferred funds (Qureshi, Volume 2:2 2017). Money laundering is as ancient as money itself, and it wasn't until much later that it was considered a crime. It is the process by which money obtained illegally is converted into lawful assets. The term 'Money Laundering' originated in the United States and referred to the Mafia's attempt to convert ill-gotten (Zubair, 2013) money into legitimate assets using various techniques. Because of the enormity of the implications, it has been designated a crime all over the world. It is interlinked with other offences and crimes (Linde, 2013) because the untraceable funds are used by terrorist organizations or criminals for their criminal purposes (Richards, 1998). Trading, Wire transfers, smuggling, credit card payments, drug trafficking, etc are some of the ways it is carried out (Manual on Countering Money Laundering and the Financing of Terrorism). The process involves three steps, beginning with placement and progressing to layering and finishing at integration. Michel Camdessus (Former Managing Director of International Monetary Fund), on the other hand, predicted that laundered money is roughly equal to 55 per cent of global GDP (Gross Domestic Product) per year, including all countries. According to United Nations' officials, the global annual figure for terrorist financing is much more than

$2 trillion US dollars (United Nations Office on Drugs and Crime, n.d.). Money laundering is linked to a variety of methods and a high level of covertness, making it impossible to anticipate the total amount of money laundered globally. The global community has concluded that extremism and terrorism cannot be combated until money laundering is controlled.

2. Stages of Money Laundering

Money laundering occurs in three stages. The funds are first deposited into a bank account in any intended foreign country. The goal of this relocation is to avoid the country's law enforcement authorities. This is referred to as fund placement. Typically, the person seeking such transfers, does the placement secretly to keep the original source undetectable. The second step is to make multiple transactions to and from that bank account in order to conceal the source of the funds (Petruzzi, 2014). This is known as layering. Internet banking and wire transfers are the most efficient ways to layer cash (Banks, 2016). Integration is the final stage in the process of money laundering. Integration is defined as the placement of laundered funds in a financial system that appears to be legitimate and clean. The potential of anti-money laundering authorities to track down the source of money becomes more difficult at the point of integration. The money that has been laundered can now be used anywhere after it has been integrated. Now it is possible to invest such money in that foreign country or returned it to the parent country as a legitimate asset.

3. Methods of Money Laundering

To fully comprehend the system's flaws, a thorough examination of the methods used by money launderers and smugglers is needed. There is an explanation of some of the methods they use to commit such crimes.

a. Smuggling of Cash

Smuggling is termed as the infamous act of moving something illegally over state borders in order to avoid paying the proper tax. This can be accomplished by deceiving border management and airport staff. Typically, large sums of money are smuggled to a country with lax financial laws and ineffective enforcement. This effectively aids smugglers and money launderers in choosing destinations where lenient anti-money laundering regulations (Albanese, 2013) prevail.

b. Trading and trade Invoices

ML can also be done through trading. It generally occurs when trade invoices are purposefully inflated or under-priced. Using this method, traders launder money to foreign nations by presenting authorities with forged (Baker, 2005) invoices and transferring the desired amount without being detected by anti-money laundering agencies.

c. Structuring of money/Smurfing

A large sum of money is divided into small sums and then easily laundered using this method. The goal of dividing a large sum into smaller ones is to make it non-taxable (The amount of money with which a person can travel without being taxed) so that it can be taken abroad without restriction. Money launderers utilize this approach to move cash around the world and deposit it in foreign financial institutions or banks. Such a method is called smurfing, and it can be easily carried out through wire transfers or physically. In practice, if a group is travelling together, smurfing is done by pretending to be strangers to one another while each member carries the highest amount of the money with which they can lawfully travel (Baker, 2005) to escape the airport regulations.

d. Non-Government Organizations (NGOs)

Regrettably, ML is often carried out under the pretext of social service, or non-governmental organisations. The procedure entails forming an NGO in a region and funding it from other countries. Anti-money laundering authorities are lenient in monitoring such NGOs that exist solely to facilitate money laundering. The motive for using a non-profit charitable organisation for laundering money is that global social standards dictate that money given to NGOs should be non-taxable (Joseph J. Cordes, 2005), for that purpose, corrupt officials and businessmen send the money and funds in the name of charity to avoid anti-money laundering authorities.

Some other techniques used by money launderers include round-tripping, operating cash-oriented businesses, controlling banking channels, unregulated foreign exchange companies, real estate, etc.

4. Implications of Money Laundering

Money laundering has a vast impact on the socio-economic framework (Qureshi, Volume 2:2 2017). It has an impact not just on a country's economy, but also on a region's overall economic framework that is severely deteriorating the global economy. It erodes a country's economic growth capacity, with potentially massive consequences. It is a social as well (Masciandaro, 2017) as an economic evil. The major consequences of this threat are explained next.

4.1. Economic Impacts

Money laundering undermines the government's capacity to oversight national economic policy and the government's ability to implement financial programmes and policies in their totality becomes very challenging. Several other issues arise as a result of the lack of implementation. Its economic impacts are not contained within a country's system; rather, due to globalisation, has far-reaching consequences that extend beyond national borders and regions. If massive amounts (Novis, 2011) of money are laundered, it can harm currencies, monetary systems, and economies around the world.

4.2. Social Impacts

Money laundering affects all aspects of society; it not only has an impact on a country's economy but is also at the root of many social crises and challenges. Financial institutions' credibility and reputation suffer when the global community come to know that the country is lax in implementing AML (Anti-Money Laundering) laws. When businesses and investments begin to contract, the social consequences are enormous. This exposes a country's citizens to other crimes such as smuggling, drug trafficking, tax evasion etc. The gains of crimes are subsequently utilised to fund additional illicit ventures by drug lords, hardened criminals, and smugglers. Other criminals are encouraged and motivated to engage in money laundering because of their impunity. As a result, ML fosters crime in society, and the entire community suffers as a result of those activities.

4.3. Pakistan and Money Laundering

Money laundering is firmly entrenched in Pakistan (IMF, 2009), and the nation is regarded as a golden crescent (Kukreja, 2003) for financial illegal activities such as TF and ML. This problem has infiltrated our social and economic indices due to a number of causes. It thrived because powerful political and influential figures participated in the conversion of their ill-gotten money into lawful assets through money laundering (Peter Muchlinski, 2008). The previous governments have remained reluctant to devise any effective action plan to culminate the looming threat of the above-mentioned crimes (Qureshi, Volume 2:2 2017). Drug smuggling in and out of neighbouring countries such as Afghanistan, India, and Iran amounts to shaky border management (International Narcotics Control Strategy Report, 2010). Several laws were passed, but they were never implemented in their entirety.

5. Money Laundering in Pakistan: Sources and Channels

Pakistan has historically been ineffective in adopting stringent anti-money laundering rules and regulations, posing a significant danger not only to Pakistan's national economy but also to the world economy. The methods of money laundering depend upon the prevalent circumstances of the country and vary from nation to nation and region to region. In Pakistan, a variety of methods or channels are used to commit above mentioned financial crimes.

5.1. Corruption Among Political Leaders and Officeholders

Unfortunately, the officeholders whose job it is to prevent and protect the economy from financial imbalances are complicit. Corrupt leaders, Administrators and politicians have always aided and abetted perpetrators in their efforts to commit money laundering, corruption, and other precursor crimes, as well as to clean their black money (IBP USA, 2018). Such officials, whether explicitly or implicitly involved, facilitated bribery, smuggling, corruption and drug trafficking.

5.2. Drug Trafficking

Pakistan is bordered by Afghanistan, India, and Iran, all of which have considerable opium or drug production (Sub-Directorate, Interpol Drugs, 2007). These borders are porous and poorly guarded; as a result, drug trafficking occurs regularly across these borders. The drug lords use the proceeds of the drug trade, which they obtain by smuggling drugs across the border, to fund other criminal or terrorist activities.

5.3. Online methods of Transactions

The significant increase in laundered cash figures is due to rapid advancement in information technology. Electronic payment methods made it easier for money launderers to wire funds and ensure the availability of funds to terrorists for criminal purposes (Criminals move with the times: Money launderers and terrorism financiers go online, 2014).

5.4. Hundi and Money Laundering

In Pakistan and other neighbouring countries, Hundi is a key money laundering method (Lilley, 2003). In Pakistan and India, hawala/hundi is a common form of money exchange. In this method, Hundi's representative in one nation receives cash from the sender and, instead of transferring the funds, asks Hundi's representation in another country to pay the money given, thereby avoiding the proper banking channel. They avoid paying the applicable taxes on the cash through Hundi, and the banking channels bear the loss. As a result of the absence of monitoring on such unlawful transactions, a large sum of money is laundered, posing a serious threat to the economic system. Regrettably, the amount of money sent each day using this means has exceeded USD30 million (Malkham, 2019).

5.5. Tax Evasion and Money Laundering in Pakistan

Pakistan's ruling elite, like that of other countries, did not bother to pay taxes (Fuentes-Nieva, 2014). They frequently commit other crimes to commit tax evasion. Typically, they bribe tax officials, allowing them to avoid paying taxes (Malik, 2010). After paying the bribe, which is usually a small portion of the taxable amount leads to low tax collection. Government officials' salaries, on the other hand, used to be dismal, making it impossible for them to live a luxurious or even comfortable lifestyle. As a result, the bribe entices them to meet their needs and such culture ranked Pakistan highest in terms of the prevalence of bribery in South Asia (Husain T. , 2016). Furthermore, anti-money laundering authorities are bribed with a large sum of money and in return allow the transfer of cash abroad. Resultantly, such detrimental culture of bribery is a key source and channel of money laundering in Pakistan.

6. Money Laundering and Terror-Financing: What's the Connection?

Money laundering and terror financing are inextricably linked. Terrorism cannot occur without considerable cash thus terrorists require funds to carry out their designs. Sponsors or benefactors of terrorists who used to be drug traffickers, the ruling class, politicians, or money launderers utilise their earnings from criminal activities to finance terrorist activities (Qureshi, Volume 2:2 2017). Various anti-state terrorist organisations and foreign extremist elements are involved in money laundering and terrorist financing (Kumar, 2002). Several foreign entities, including Blackwater, RAW (Research and Analysis Wing is the intelligence agency of India), and the CIA (Central Investigation Agency is the Intelligence

Agency of USA), have been involved in the financing of anti-state groups and terrorists (Draitser, 2014) in Pakistan (IMF, 2009).

The arrest of former RAW official, Kulbhushan Yadav, who was found operating a terrorist network in Pakistan, clearly illustrates the Indian interference and involvement in terrorism. He admitted to carrying out terrorist activities in various Pakistani cities, primarily Quetta and Karachi (Shah, 2016). It appears to be the explicit involvement of foreign extremist elements who spent a lot of money to tarnish Karachi's peace, and the aftershocks are still confronting people.

6.1. Major Gaps in Pakistan's Legislative System

Money laundering is an offence in Pakistan, according to the *Anti-Terrorism Act 1997* (Section (11)(k). The act aims to combat terrorism and its financing by seizing, freezing, and forfeiting assets generated from the crimes listed. The *Control of Narcotics Substances Act 1997 (CNSA)* also included the offence of ML in it, allowing prosecution agencies to forfeit and freeze assets obtained from psychotropic substances and narcotics. Pakistan implemented several measures with the gravity of regulations in 2003, demonstrating its commitment to fighting money laundering. Simultaneously, the State Bank of Pakistan, which oversees Pakistan's monetary and credit systems, formulated and released *"Prudential Regulations M1 to M5"* (Ali I. , 2019), further amended in 2016 to limit the risk of money laundering to prevent banks from this menace (State Bank of Pakistan, 2018).

6.2. Review of Legislation

Since 2000 Pakistan has been a member of the Asia Pacific Group (FATF's regional organization tasked with combating money laundering and terrorist financing), making it obligatory to enact comprehensive anti-money laundering legislation in accordance with international standards. *The Anti-Money Laundering Ordinance* was enacted in this regard in 2007, although it has been plagued by faults from its inception such as money laundering was designated as a non-cognizable offence, and only a few predicate offences were added to the AMLO schedule.

The Anti-Money Laundering Ordinance was repealed in favour of the Anti-Money Laundering Act 2010, which made substantial improvements for the better. It includes a detailed preamble as well as an expanded definition of Money Laundering. The mandate and scope of the Act were enhanced by adding the provisions to combat money laundering and terror financing, and the provisions were also added according to which, authorities can confiscate and attach the assets gained through ML or other criminal sources. Notwithstanding these meaningful provisions in AMLA, it is riddled with loopholes and gaps that must be filled. The prevalence of the *Hawala and Hundi* networks in Pakistan is the most common method via which offenders engage in money laundering. It is one of the most convenient methods of sending money to some other country without physically moving it. The pervasive gaps in present legislation do not prevent these illicit organisations from operating (Farooq, 2018).

6.3. Investigating and Prosecuting Agencies

Initially, three authorities were given the power to investigate and prosecute offenders under section 2(j) of the AMLA.: the *National Accountability Bureau*, the *Anti-Narcotics Force*, and the *Federal Investigation Agency*. Following that, the Ministry of Finance and Revenue also designated the *Directorate General Federal Board of Revenue* as the prosecuting agency on August 24, 2010. The irony is not unusual to the Pakistani system; NAB which is governed by NAO, has jurisdiction throughout Pakistan, but it lacks the authority to investigate and punish AMLA offences. The reason for this inaction is that Money Laundering and its precursor crimes have not been incorporated as scheduled offences in the ordinance. The AMLA seeks to prevent the laundering of money, and financing of terrorism and confiscates or attaches moveable and immovable property obtained from the proceeds of such acts. Contrary to Anti-terrorism Act (ATA), NAB is unable to prosecute and conduct an investigation, as such crimes are not predicated offences in its Law.

The *Federal Investigation Agency* is the second agency that AMLA has designated as authorised to investigate and prosecute its scheduled offences. As per the preamble of the FIA Act 1974, the agency's duties are confined to investigating offences involving the Federal Government and establishing an embargo on the FIA's authority. As a result, it is unable to work and investigate issues at the provincial level, as well as crimes committed by private individuals. ATA is listed in the schedule of FIA's Act. But the agency has an Inter-Provincial scope, and it only investigates those cases handed it over by the Federal Government. Another hindrance is that the FIA lacks considerable authority to take the necessary steps to prevent the aforementioned offences.

The '*Anti-Narcotics Force'* is also an agency to investigate and prosecute the offences in AMLA. The governing law of the force is 'The *Control of Narcotic Substances Act 1997'.* But, the agency is only mandated to limit and control narcotics and drugs-related offences.

Finally, the *Federal Board of Revenue's Directorate-General (Intelligence and Investigation Inland Revenue)* is an AMLA investigating agency, having the jurisdiction to conduct an investigation and prosecute its predicate offences.

The situation concerning investigative and prosecuting agencies differs greatly in other countries. In India, for example, there is just one specialist body to investigate financial crimes, the *Directorate of Enforcement*, which is part of the Government of India's Department of Revenue. Similarly, the *Joint Money Laundering Intelligence Taskforce* in the United Kingdom, which is part of the National Crime Agency, is tasked with investigating financial crimes (Madinger, 2011).

7. Conclusion

This study defines and elaborates on the term money-laundering. It explored different methods of money laundering used all over the world. The study then finds out the different implications of money laundering, especially for developing countries like Pakistan. It discussed the economic and social implications of money laundering for Pakistan. Money laundering is specifically discussed concerning Pakistan with the most commonly used sources and channels of money laundering in Pakistan. In the last part, this study described the major gaps in Pakistan's legislative system along with current legislation and framework dealing with crimes of money laundering.

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