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Essay Title: **Global Governance**

Essay Number: **1**

Module Code: **PUBL0061**

Module Title: **Global Governance: Policy Brief**

Submission Date: **18 January 2023**

Word Count: **2880**

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TO: Ms Nirmala Sitaraman, Minister of Finance and Corporate Affairs of India.
FR: BRVD7
DA: 18 January 2023
RE: Addressing the economic issue of Money Laundering and Terrorism Funding at G-20 summit.

Abbreviations

G-20 - Group of 20 Nations.
ML- Money Laundering
AML- Anti Money Laundering
FATF- Financial Action Task Force
FIUs- Financial Intelligence Units
JWC- Joint Working Committee

Introduction

It is clear how important it is for a nation to develop its economy from Adam Smith's comment that "no society can undoubtedly be prosperous and happy, of which the far larger portion of the people are destitute and wretched." Because per capita income, which ultimately measures an individual's economic success, is one way to judge the economic growth of a nation. Therefore, it cannot be denied that the economy has an impact on the world we live in. Concerns like tax and inflation, wealth and interest rates, inequality and developing markets, and energy and the environment are included in this.As the world continues to expand, so do some of the key global economic challenges. Money laundering is one such unspoken issue that has the potential to have an equal influence on economic progress. The biggest concern in the world economy has always been money laundering, although being relatively neglected. Financial institutions, which are essential for economic growth, are negatively impacted by ML, and resource misallocation caused by ML also has a detrimental effect on economic growth. Research has also supported these assertions (Quirk, 1997). In a study of 18 industrialised nations conducted between 1983 and 1990, it was shown that ML increased in correlation with a decline in economic growth.

The majority of money launderers, as according Bartlett and Breeden (2002), choose to invest in companies that offer the maximum level of deception over enterprises that make significant profits. These expenditures divert resources to projects that provide little economic activity and jobs, which might be harmful to the economy. The main sources of money laundering (Colombia affair, 1980s) are similarly fraudulently inflated land values. Additional In order to insure some high-value items, criminals purchases a general insurance policy using filthy money. Additionally, shady money had been used to purchase these items. They then filed a false claim against the insurance. As a result, they effectively used the insurance firm as a money laundering scheme multiple times. Therefore, the largest predators who are at high danger from these sandals are banks, real estate firms, and insurance businesses. Such organised financial crime may cause economic distortions by lowering tax revenues, interfering unfairly with legal enterprises, harming financial systems, and halting economic growth.

The ongoing COVID-19 coronavirus epidemic has caused a major instability in the world economy by spreading rapidly across the globe. A nation's import and export activities were greatly affected by the pandemic, which resulted in a higher inflation rate and had an impact on economic strategy and management (AL-MANSOUR, 2020). There have been several money laundering and corruption scandals associated to COVID-19 that have occurred throughout the epidemic, according to an updated study by FTAF titled "COVID-19-associated Money Laundering and Terrorist Financing." The UN estimates that around $1.6 trillion is laundered annually, and officials claim that lockdown measures have given criminals even more possibilities to perpetrate crimes. With the exception of money-laundering, the coronavirus epidemic has severely restricted commercial activities during the past three years. Lockdown measures, according to FATF, a watchdog group for financial crime, have given criminals more chances to conduct crimes involving the laundering of millions of dollars' worth of gains (Financial Times). Therefore, this element has also played a role in the worsening of the prognosis for the world economy. Such illegal acts now have another outlet due to the Internet. Money launderers are now able to instantly and discreetly transfer money across international boundaries owing to a practise commonly referred to as "digital transfers" (New Straits Times, 2002a, February). The pandemic has acted as a trigger for such cybercrimes. According to the deputy finance minister Datuk Dr. Ng Yen Yen, an international survey found that such fraudulent operations cause banks to lose 10 times as much money as heists (Business Times, 2004a,b,c, September)

Money laundering is a significant issue on a worldwide scale not just because it is an economic issue but also because it is linked to the most important national security problems. Money laundering is one of the main ways that Terrorism is funded. So, from the standpoint of good global governance, ML prevention becomes crucial.

Why India and G-20?

It is undeniable that FATF is a major player in the battle to combat money laundering on a worldwide scale. By following the necessary FATF guidelines and policies, it has shown that nations has started to take measures or policies to reduce their risks. Over 80% of FATF member nations' responses have been considerable or highly successful, demonstrating that they have a thorough grasp of risk. The operation of the FATF and its member nations, however, still lacks the necessary competence. Thus is because of the conspicuously ignored gridlock in the system.

First off, India's information technology and software sector is currently a worldwide powerhouse with immeasurable effects on the country. It has made a significant contribution to promoting India as a desirable investment destination among foreign investors and expanding job prospects there. Other than that, India holds the presidency of G-20 for 2023. Thus, it is vital that it confront the problem of money laundering now.

Secondly, FATF mainly executes its policies on member nations through publishing recommendations known as "FATF Recommendations," which are not legally enforceable. The Group of Twenty (G20), on the other hand, is the most important platform for global economic cooperation. It contributes significantly to the development and reinforcement of the global governance over international economic challenges. Here, conversations takes place at one of the major forums which hosts the greatest economies in the world. Hence G-20 can act like a bridge to overcome the limitations of FATF in making one countries to indirectly comply by certain laws, through meetings and discussions, in order to meet the general requirements for combatting ML. Hence, mentioned below policy briefs are recommended to be discussed at G-20 summit. As India hols the presidency of 2023, it share the responsibility to highlight this major economic concern.

Policy Recommendations

First policy Recommendation.

In combating money laundering, I will represent a significant gridlock trend between G-20 countries and the FATF. Simultaneously, I will make policy proposals for G-20 countries, as well as some guest countries, to combat money laundering successfully. This policy brief focuses mostly on G-20 nations because they are the world's largest economies, accounting for around 85 percent of global GDP.

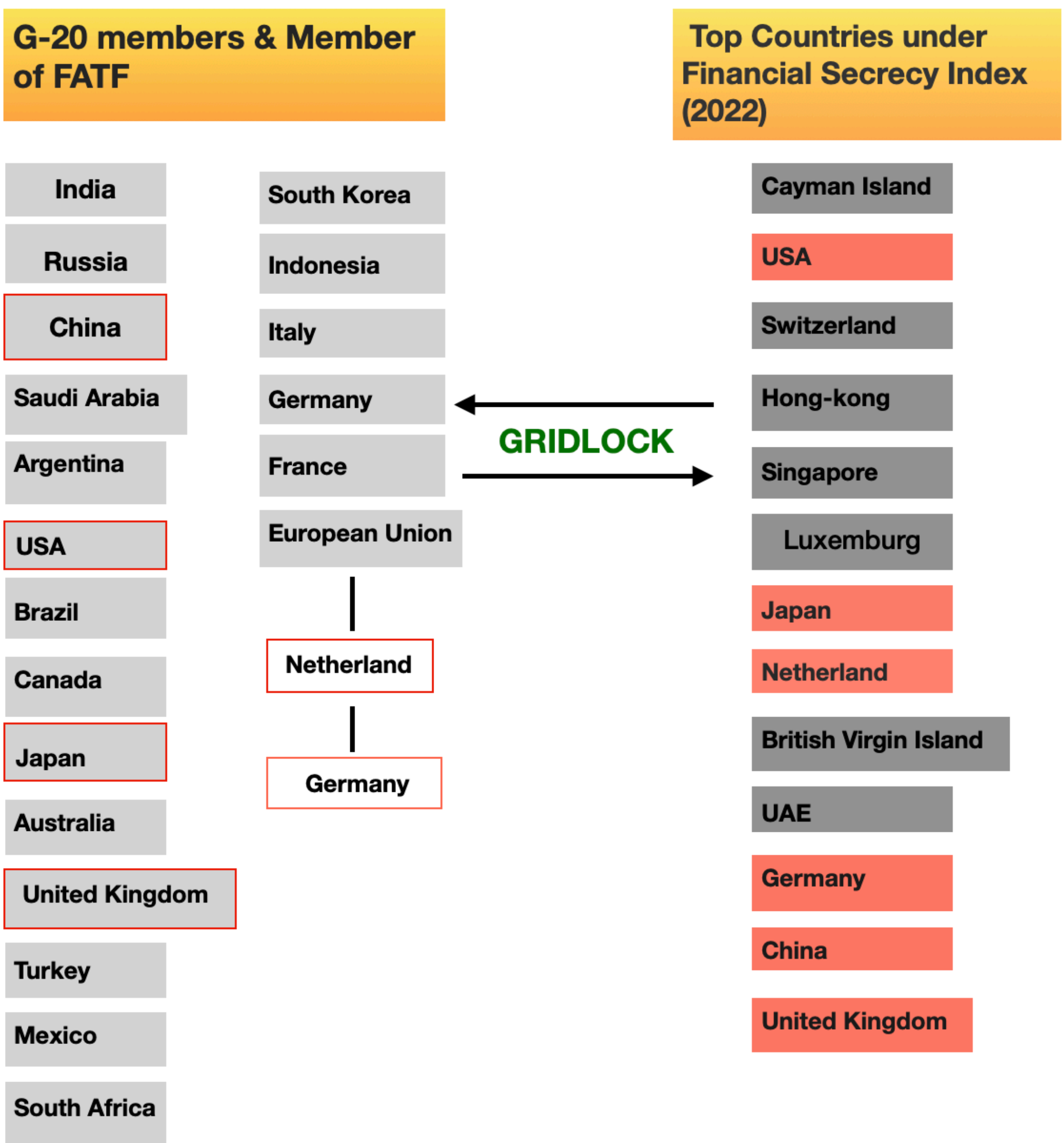

Fig-1.1

Referring to fig. 1.1, the first column lists the countries that are members of the G-20. Despite this, all of these countries, along with an additional 19, are FATF members. The FATF's 10th provision of Customer Due Diligence was a crucial recommendation. Know Your Customer, or KYC basically, is the process of evaluating the risks posed by both current and potential consumers. KYC procedures aid in preventing financial crimes such as identity theft, money laundering, financial fraud, financing of terrorism, and others. Surprisingly, every G-20 and FATF member country except for Netherland has successfully incorporated KYC into their regulations.

Recommendations 36–40 of International cooperation are one of the FATF's other key recommendations. Mutual legal aid is a key component of this internal cooperation recommendations. The FATF recommends that countries should provide the widest possible range of mutual legal assistance in relation to money laundering, terrorist financing, investigations, prosecutions, and related proceedings. But lot of nations have not yet taken this recommendation seriously. According to the Tax Justice Network's Financial Secrecy Index (FSI), several nations who are members of the G-20 , FATF and, have regulated KYC, have also secured their positions in the top 15 under FSI. These nations with the highest ranks are less transparent in the activities they host, less involved in exchanging information with other national authorities, and less compliant with international money-laundering regulations. Due to its inability to engage in effective information sharing, a secrecy jurisdiction is more desirable for channelling unlawful money flows and thus concealing criminal and corrupt behaviors (European Commission report: 2020).

This is a major gridlock because there are some countries members of FATF which have not yet complied with this particular recommendation 36-40. The G-20 may be the most hopeful platform for discussing such deadlock tendencies. If these countries chose to keep silent, it will not only cause economic instability in other countries, but they will also have to pay for the repercussions at some time. Because of this gridlock, many scandals are unreported, despite the fact that the FATF operates very effectively, due to its own members' financial secrecy laws.

<u>Second Policy Recommendation</u>

When reporting any fraudulent monetary crime, accountability must be accurately identified from the top down approach. Members of society are accountable to society, banks are accountable to society when they are allowed to function in the banking sector, and workers are primarily liable to the bank when they implement its risk assessment models. This exemplifies the conventional type of (vertical) responsibility. Furthermore, it can be fostered horizontally, such as collaboration between nations and supervisors, or cooperation between banks.

All countries execute national policy, which implies that businesses, government agencies, and others must follow the same rules. Similarly, one thing that may be ensured is that AML that is, Anti-Money Laundering laws of one country does not differs widely to AML of another country. This argues that in order to prevent gridlock, all member countries' basic fundamental AML legislation should stay consistent. Therefore, second policy recommends that the country's AML must have these 4 essential components in line with FATF recommendations.

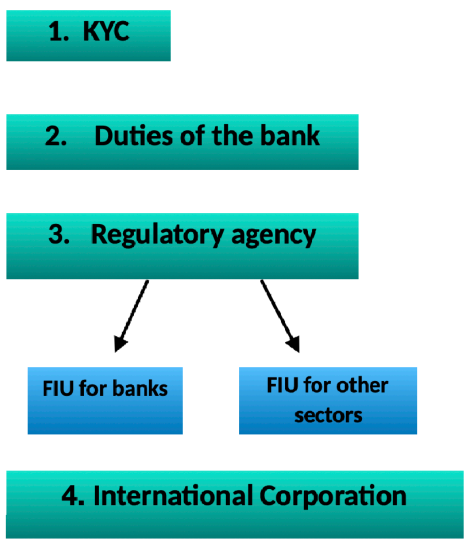

Fig-1.2

The first recommendation in the policy brief clearly explains the importance of KYC:'Know Your Customer". As a result, each member country must ensure that this component is included in their national AML.

There must also be assurances that banks and issuers adhere to AML requirements (Financial Supervisory Authority, 2020b). The goal of this oversight is to guarantee that banks do not engage in money laundering. Bank-specific risk assessments on money laundering concerns are established by the Financial Supervisory Authority under FIUs by gathering data on risks and controls from the banking and insurance sectors that are subject to supervision. The risk-based approach is based on the fact that money laundering cannot be completely prevented, but prevention measures should be targeted where the risk is greatest. Banks and other whistleblowers have statutory obligations to stop money laundering. These obligations include the duty of knowledge, the duty to report, the duty of care and the duty to follow a risk-based approach. The sense of imposing 'Duty' leads to an indirect obligation of abiding by the rules. Finland, a well-known and top-performing country in the fight against money laundering, undertook such initiations.

There currently exists a committee of Financial Intelligence Units under each nation's regulatory agency (FIUs). This policy brief recommends that this FIU be split into two sections. This way, it will be easier to understand who is responsible for what and track financial scandals more effectively with division.
A portion of FIUs must be cast aside solely for the banking and insurance sectors. (FIU for Banks) Due diligence procedures should be followed in this case whenever a financial institution begins a new business relationship, when particular types of transactions occur, when there are questions about the customers' identities, and when there is a possibility that money laundering and/or terrorist financing is taking place.
Steadily from the past, as nations have tightened rules and increased oversight of financial institutions, criminals have discovered ways to exploit other, less regulated industries to launder their money. As a consequence, the FATF advises that countries employ these remedies and diligence in non-financial sectors like real estate, microbusinesses, and macrobusinesses, as necessary, and continue to be alert to new threats. It thus will be the FIU's for other sectors.

The fourth component discusses the international corporations that are indicated by FATF recommendations 36 - 40 and briefly covered in the first recommendation of this policy brief. Many nations have not yet complied with this requirement, which has caused a deadlock. Therefore, it is imperative that this specific issue receives the most attention in the G-20 international summit. Laundered money travels through various sources around the world. Therefore, there must be unquestionably the greatest cooperation between the nations for sharing some encrypted information, with proper prudence, in order to confront this significant challenge of money laundering and terrorist funding.

Third Policy Recommendation

After every fixed interval of years, the FATF performs a peer review of each nation to examine the level of implementation of the recommendations and to give an in-depth analysis of each country to avoid criminal misuse in the financial system. The report that they create for each country is known as an evaluation report, and it takes 18 months to accomplish.
Thus, in order to strengthen domestic actors' cooperation, I propose that a Joint Working Team (JWC) must be formed in each nation that is a member of FATF and the G-20 before the FATF

review report is released. This (JWC) will be made up of three representatives from each department, namely the Enforcement Directorate, the Income Tax Department, the Directorate of Revenue Intelligence, Financial Intelligence Units (banking and non-banking sectors), the Banking Regulator (Central Bank), and the Insurance Regulator. JWC will prepare a report and offer it to a FATF expert. The report they prepare would include all necessary activities taken to prevent money laundering in their country, as well as ongoing status after implementing such legislation. Aside from that, the report will discuss the shortcomings and limitations of the country's regulations. This creates a mutual partnership of all required intelligence agencies at the national level. The key goal of bringing in diverse organisations from banking, insurance, real estate, and other industries is to keep checks and balances on the reports they will be representing. Thus, the assessment report prepared by nation and then FATF will provide a 369 degree overview on where exactly a nation stands in dealing with the problem of ML and terrorist financing.
The actual data that supports this type of structured committee and how efficiently it functions comes from India, when its FATF review report was delayed due to pandemic, until sept 2022 (Economic Times, The Indian Express, India FATF portal).

Limitations of policy recommended

This policy proposal aims to be free of any potential economic drawbacks. However, there is a good likelihood that these recommendations may raise political and legal issues for some specific countries. For instance, in a nation like Switzerland, it is a crime to reveal client information about a bank, regardless of whether doing so is in the public interest or a matter of concern for the entire world. If there are provisions of such laws, then it will be extremely difficult to expect their international corporation. It will jeopardise the policy proposed and may lead to in fact zero effectiveness in international corporation. When it comes to ethical considerations, it seems a little bit unethical to disclose all of the personal information of regular individuals to other nations. The common people are placed in a precarious situation where anyone may view their personal information. However, this circumstance is manageable. Governments have a responsibility to ensure that the data they have on their citizens is highly protected and that only information on significant international frauds is disclosed outside of national borders.

Conclusion:

Although the intergovernmental structure that is evident in relation to the FATF and AML is certainly very well structured, it is crucial that some improvements be made in light of the expanding global community. Consequently, there is no need to entirely rebuild the system to tackle money laundering. Instead, this policy proposals explains new perhaps updated policy recommendation in the pre-existing design by shift in the paradigm to maintain its efficacy

The largest democracy of the world is in India. The nation's economic expansion has coincided with its incorporation into the world economy during the past ten years. India now has the ability to influence global economic issues through strongly held policy suggestions since, it has become a major actor on the world stage. Nevertheless, The G20 is crucial in fostering an atmosphere that promotes equitable global growth and development. There is no better opportunity for India to speak out against the economic problem of money laundering than now, while it is in charge of the G-20 presidency. As the slogan of this year’s presidency is global unity:’ One Earth, One Family, One Future’, If Ms Sitaraman and India wants to retain its audacious self-styled reputation as a ‘economic powerhouse’, then they must act boldly on the world stage.

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