BUSINESS RECORDER
Founded by M.A. Zuberi

Getting rid of money laundering

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The new coalition government led by Prime Minister Imran Khan's Pakistan Tehreek-e-Insaf (PTI) seems determined to break the socio-economic and political status quo that has kept Pakistan entrapped in a stifling growth mode since the country's very inception.

One of the most debilitating of the side-effects of this state of affairs has been corruption. The menace has devastated the body and soul of the nation.

The money that is made through corruption - tax evasion and avoidance, smuggling, black-marketing, bribery, kickbacks, under the table commissions ,etc., - continues to expand the black economy which according to one estimate is currently equal in size to the country's white economy. Others have estimated it to be more than one-half of the size of the formal economy.

A big chunk of this money is continuously laundered out of the country and gets lost in tax havens and through them turns into white and part of it comes back home mostly in the shape of remittances.

The current government which wants to eliminate corruption from Pakistan, needs to simultaneously attack the very sources of corruption in the country as well as trying to curb the menace of money laundering which is also carried out by foreign trade over- and under invoicing. And also at the same time it needs to mount legal efforts to bring back home all the tainted money that has been siphoned off from our legitimate economy over the past over 70 years.

Tracing the trail of tainted money from origin to final destination has become an extremely complex proposition because most of the black money normally is camouflaged in more than two dozen jurisdictions up-loaded in far-flung networks of trusts, shell corporations, and foundations to conceal it from tax authorities and law enforcers.

Wealth managers not only exploit gaps in legal systems but also seek to influence legislation, especially in offshore tax havens, to the benefit of their clients. In doing so, they help undermine the legitimacy of governments that tolerate their wealthy criminals' evasion or avoidance of the financial responsibilities and corruption.

In view of these complexities and also because most of such tainted money is owned by the policymakers themselves in Pakistan who are also the main implementers of these policies they have most of the time resorted to amnesty schemes claiming that the move was being made to curb expansion in the black economy. However, such schemes have helped whiten only a small fraction of the black money while at the same time served to penalize the honest taxpayers.

All the tainted money is not hoarded in cash. In fact, most of it is held in goods, in clandestine businesses, in real estate, in secure currencies like dollars, pounds and euros and in gold and jewellery.

Money laundering is the process that disguises the proceeds of crime and integrates it into the legitimate financial system. There are countless ways to launder money. For example, a criminal earns $1 million in cash from tax evasion in Pakistan. This cash is smuggled across border, placed in a bank account. From here the money is wired to account owned by an anonymous shell company. It is finally integrated into white money when the shell company buys real estate in Pakistan or anywhere in the world for the client.

The global fight against money laundering and financial crime continues unabated and cash, in the form of high-denomination bank notes, is also being targeted.

Experts believe Pakistan could also make it more difficult for the corrupt to move their tainted money if the State Bank of Pakistan were to just stop issuing currency notes of Rs. 5000 denomination and let those in circulation taper off over a fixed period of two- to three-years without actually demonetizing these notes.

A March 2017 report by Global Financial Integrity (GFI), “Transnational Crime and the Developing World,” evaluates the overall size of criminal markets in 11 categories: the trafficking of drugs, arms, humans, human organs, and cultural property; counterfeiting, illegal wildlife crime, illegal fishing, illegal logging, illegal mining, and crude oil theft. Counterfeiting ($923 billion to $1.13 trillion) and drug trafficking ($426 billion to $652 billion) have the highest and second-highest values, respectively; illegal logging is the most valuable natural resource crime ($52 billion to $157 billion).

Despite recent progress, there are still plenty of places all over the world where one can stash one’s money without fear of being found out. Tax havens aren’t tax havens just because they have low taxes — rather, what makes a tax haven is its opacity of financial information. This is why tax havens are often more accurately referred to as ‘secrecy jurisdictions’ and why they facilitate many more problems than just tax evasion.

While the legal regimes that tax havens set up to enable this secrecy are complex, their basic outline is simple—banks, companies, trusts, or other financial actors in the country are allowed to accept money from basically anywhere without reporting it to the authorities in the country where it originates or from which it is controlled. In some cases, it is actually illegal to disclose that information, but in many places, it is simply because the banks or other entities aren't required to disclose it and there is no mechanism to force them to do so.

Laundering criminal proceeds through a tax haven is therefore merely a matter of finding a bank in that country to accept your deposit without asking questions, shuffling the money around a bit, and then sending it to wherever you'd like to spend it or to wherever you'd like to receive it. Evading taxes through a tax haven works similarly—disguise income or assets as passing through that country and fail to report it to your home country's tax authority.

For the less criminally inclined, tax havens often also offer a great legal way to avoid paying taxes, simply by characterizing income as passing through that country and using loose tax treaties or loopholes in one's home country tax law to claim that the income is un-taxable there.

What is needed to curb this practice is a law requiring automatic exchange of financial information. Countries need to automatically exchange information on bank accounts, transactions, and financial flows with each other on a periodic basis, enabling law enforcement and tax authorities to follow up on any leads they may have.

The G20 nations declared in 2013 that automatic exchange is "the new global standard," and pledged to begin exchanging financial information automatically by the end of 2015. In 2014, every OECD member-state and a group of several other countries endorsed a standard system for multilateral automatic exchange of financial information.

GFI believes that any multilateral system of automatic exchange should also serve the interests of the world's smaller economies, but must also take into account the capacity of these countries to effectively utilize the data they would receive from this system. Technical assistance and capacity-building programs will be crucial to this effort, but developed countries should also consider exchanging information to developing countries without obligating them to return the favor, at least initially.

GFI recommends that all multinational companies be required to publicly disclose basic financial information, such as their sales, profit, taxes paid, and number of employees, in each individual country in which they operate. This policy, called "country-by-country reporting," will not only help both rich and poor countries better enforce and amend their tax laws, but it will also make free markets more transparent for investors and the public at large.

Transparency International's latest report, 'Exporting Corruption', names the top offenders as well as the flaws in national legal systems that allow corruption to continue unchecked. Take, for example, foreign bribery. It has huge negative consequences for the economies of the nations targeted. Money gets wasted on deals that are overpriced or do not yield real benefits. Limited resources are diverted to benefit a few individuals while citizens are denied vital public services, such as access to clean water, safe roads or basic health services.

According to the World Bank, businesses and individuals pay more than $1 trillion in bribes each year.

Citing World Economic Forum estimates that corruption costs at least $2.6 trillion – or five per cent of global gross domestic product, the UN Secretary General António Guterres told the Security Council on Monday (Sept. 10, 2018) at a session on tackling corruption for the sake of peace and international security that numbers show the startling scope of the challenge.

Guterres elaborated saying that corruption:

• Robs schools, hospitals and others of vitally needed funds.

• Rots institutions, as officials enrich themselves or ignore criminality.

• Deprives people of their rights and drives away foreign investment and despoils the environment.

• Breeds disillusion with government and governance – often at the root of political dysfunction and social disunity.

• Can be a trigger for conflict.

• And, drives and thrives on the breakdown of political and social institutions.

“The poor and vulnerable suffer disproportionately,” he stressed. “And impunity compounds the problem.”

The UN chief linked corruption to many forms of instability and violence, such as the illicit trafficking of weapons, drugs and people and noted that connections between corruption, terrorism and violent extremism have been repeatedly recognized by the Security Council and General Assembly.

“It is especially important to build up the capacity of national anti-corruption commissions and prosecutorial efforts,” he told the Council, encouraging governments to ensure independent judiciaries, media freedom and whistleblower protections.