Money Laundering: A Globalized Problem

Introduction

The economic problems have taken a global dimension after globalization. Necessarily, it has also increased the supply chain of products across the borders. Cross-border transaction of black money and money laundering are serious economic crimes, and it causes substantial impacts on the economic development of the world. Illicit trade is the fountainhead of these problem, and estimated total cost of illicit trade is $ 1.77 Trillion in 2015 which is about 10 percent of global trade in merchandises (World Economic Forum 2015). Both crimes associated with corruption and the combat against these problems demands both local and international actions. United Nations Office on Drugs and Crimes (UNODC 2019) reveals that money laundering is accounted for 2-5 percent of global GDP (Gross Domestic Product), that is the lowest estimation. UNODC is an international organization fighting against international crimes, and it depends on the voluntary contribution of governments for its 90 percent of financial needs (UNODC 2019). UNODC (2019) provides technical assistance, model legislation and needed instruments to the nations.

A globalized problem

I argue that globalization has enabled the illicit outflow of money and money laundering because diminished state control had made money laundering as a global problem.

After the end of the cold war, capitalism accessed into new territories and unprecedently established more economic integrations in the global scale (Gilman, Goldhammer & Weber 2011, p.7). Privatization programs in the post-soviet territories facilitated quick and painless mobility of state assets into the hand of private entrepreneurs, and this was a major agenda of US-centric capitalist order (Gilman, Goldhammer & Weber 2011, p.7). The deviant form of globalization that is parallel to mainstream globalization possesses an attribute that changes the problems of governing a global economy (Gilman, Goldhammer & Weber 2011, p.7). Deviant globalization has resulted in a huge amount of black money through illegal businesses such as sex trade, drug dealing, terrorism, illegal arms supply and the market for human organs.

The causes of black money are excess government intervention in the economy (via licensing and regulations), funding of political parties, a higher rate of taxes and inefficient enforcement of tax laws (Sarkar 2010, p.128-129). Vice versa, the privatization also brings new scopes to earn black money through the bribes of bureaucrats and politicians as well (Sarkar 2010, p. 129). However, tax law enforcement becomes difficult in developing countries due to its sunshine laws.

As a result, huge amounts of black money are formed in the focal points, and the money laundering also becomes a serious problem at the global level. Money laundering is the processing of profits gained by criminal activities through the financial system to disguise their origins and to make them appear clean money (Buchanan 2004, p.117). Money laundering offers chances to make the black money into clean forms and again used for their prescribed purpose in the legal business. Criminals use the advantages of globalization by transferring

funds across the borders in a quick way (UNODC 2019). Money laundering process creates burdens on the world economy by crippling the operations of national economies (Buchanan 2004, p.116). In addition, Financial markets become corrupted, risky and unstable, and finally slow down the growth rate of the economy (Buchanan 2004, p.116). Therefore, money laundering takes global dimension after the globalization.

The governments have moved toward openness of trade, finance, and investment. These changes are the prima facie evidence of a new global logic of capitalism (Weiss 2000, p.9). In this context, states become apparently powerless to make real changes in the public policies, and states have to adopt similar policies of a global trend (Weiss 2000, p.9). In addition, Weiss (2000, p.13) articulates that globalization and state power are not a negative sum game where the growth of the former can only happen at the expense of the later.

It is appropriate to examine the World Trade Organization (WTO) guidelines and research in the capital flows and financial service markets. WTO consists of 164 country members around the world since 29th of July 2016 (WTO 2019). The General Agreement of Trade and Services (GATS) is the multilateral rules and regulations governing international trade in services and, it came into effect in 1995 (WTO 2019). GATS agreement demands only limited liberalization of capital flow in terms of financial services trade liberalization (Kono & Schuknecht 1998, p.4). However, restrictions enforced on capital flows in the forms of control of capital and exchange greatly decline the freedom of choice to obtain services from foreign financial institutions, and give negative incentives to the entry (Kono & Schuknecht 1998, p.5). Therefore, practically speaking, liberalization of capital accounts and financial services are complementary in nature in the market-based economy (Kono & Schuknecht 1998, p.5).

Although Kono & Schuknecht (1998, p.32) have articulated that nations having strong macroeconomic policies, regulations and stable financial system are highly deserved to adapt very broad capital and financial market liberalization, it is indispensable to allow some sort of strong regulatory measures on capital and foreign direct investment flows to achieve full benefits rather than adapting a laissez-faire policy. In this context, while neo liberalized policies are enforced in developing countries having lack of under-developed financial system and governance, it substantially encourages a parallel economy and black market.

For brevity, illicit flow of capital and money laundering are indeed global problem by nature, and its flow across the border is a menace to the world’s economic development.

Failed Promise: Does neo-liberalization enhance money laundering?

The economic perspective of globalization prescribes neo-liberal policies to the development. Presently, the neo-liberal policy is the only available way to allocate resource efficiently with more privatization and foreign direct investment (FDI) (Friedman 2000, p.106). Nevertheless, the countries which fervently adopted liberalization policies as a remedy for past miseries show different experiences. India introduced liberalization in 1991 in the name of economic reforms. Evidently, the statistically significant correlation found between the sizable volume of illicit capital flow and deteriorating income distribution (Kar 2011, p.7) after the economic reform. Particularly since 2000, this picture sounds more prominent. Dev Kar (2011) says:

Above empirical study vividly proves that economic policies embraced during the globalization facilitate outward flow of black money, which is the source of global money laundering.

Money laundering in a legalized form: from black to white

I argue that neo-liberalization policies encourage money laundering practices because the double tax evasion treaties and tax havens provide the chances to legalize money laundering in the guise of Foreign Direct Investment (FDI).

Illicit financial flow (IFF) is the illegal movement of capital or money across the border, and the IFF afflicts the tax revenue of developing countries and undermines the efforts to achieve the sustainable development goals (Global Financial Integrity [GFI] 2019). GFI (2019) estimated that on average, 20 percent of the trade of developing countries with developed countries fall under the IFF.

The actual purpose of the transformation of black money is to convert that money into the version of legal usability (Schneider, & Windischbauer 2008, p.6). The illegally originated money is used to inject into the financial system and converted into visible assets and investments such as tourism projects, business and industrial enterprises (Schneider, & Windischbauer 2008, p.7). Newly developed technologies such as smart cards, online banking, and cyber money facilitate a very easiest form of money transaction and it also encourages money laundering without territorial and legal barriers. In this case, customer identification is extremely difficult when money laundering takes place through the internet (Schneider, & Windischbauer 2008, p.13-14).

In this context, we have to examine the role of tax havens and double tax avoidance agreements which facilitates the easiest and legalized form of money laundering. Tax havens are the secrecy jurisdictions found around the world, and anyone can deposit their cash in a very confidential manner without any scrutiny (GFI 2019). About seventy or above tax heavens serve as just booking centres of financial centres of London, Tokyo and New York (Palan 2002, p.151). A rough estimation reveals that about 50 percent of the world' money stock resides in these tax heavens or pass through them (Cassard 1994; Kochen 1991 cited in Palan 2002, p.151). Tax havens are not similar in their mode of taxation, but they have possessed some similar attributes such as effective bank secrecy laws, minimal or no corporate taxation, few or no restrictions or regulations on financial transactions and protection of the secrecy of transactions (Palan 2002, p.155).

Evidently, these tax havens can be utilized to deposit the money which was originated and safely transferred from the national borders. The strict secrecy laws of tax havens thwart the information about its customers to required countries who investigates the black money's origin.

In the studies of Slemrod & Wilson (2009, p.1261), they state that partial or full elimination of tax haves shall improve the welfare of non-haven countries. As substantial non-taxed money is deposited in the tax heavens, it results in inequality among the states. Eliminating tax havens creates two desirable effects in non-haven countries. Each countries' residents obtain benefits from resources that were used for income shifting and tax enforcement activities, and as the marginal cost of public goods declines, countries could increase the public good's provision to

their citizens (Slemrod & Wilson 2009, p.1265).

Hong & Smart (2007, p.17) suggest a different view of the tax havens. The international tax planning opportunities allows countries to keep their tax rate at the highest level and reduce the outward flow of capital. In addition, they articulate that an increase in the international tax avoidance increases both statutory and effective tax on capital and if the initial tax rate is small, it will enhance the welfare of citizens of high- tax paid countries (Hong & Smart 2007, p.17). Notwithstanding, tax havens provide opportunities to investors not to report it to the own countries' tax authorities, and to avoid paying taxes in a legal way (GFI 2019). Evidently, this situation offers the best chances to protect the black money in these havens and to use them as new investments in another country without criminalizing the investors.

Nevertheless, In the developing countries where the taxpaying rate is low, its impacts may be calamitous.

Tax Double Avoidance Agreement: No tax Burden Anywhere

Double avoidance (DTA) agreements offer a golden opportunity to the money laundering in the guise of Foreign tax Direct Investment (FDI). Many countries have rectified double tax avoidance agreements with tax havens. Therefore, while money entered into the tax havens and move outward to the country where DTA is found, so that money obtains tax concession in two points.

Economically, some arguments favour of DTA. Developing countries having more DTA agreements with capital-exporting countries, especially the USA obtain more FDI inflows and a higher share of FDI (Neumayer 2007, p.20). However, Neumayer (2007, p.21) further adds that the DTA agreements will be beneficial to only middle-income developing countries. Another study shows that the firms enjoy the privilege of reduced cost via the tax haven operation, and those firms' activities increases in non-tax haven territories due to its cost-effectiveness (Desai, Foley & Hines 2006, p.7).

Nevertheless, offshore financial centres (Tax havens) consists of numerous shell companies which conduct no business activities, and these financial centres' secrecy laws prevent the investigation of such registered shell companies for money laundering (Buchanan 2004, p.118-119). If any developing countries sign the DTA treaty with these offshore financial centres, the money laundering could take place through the shell companies from tax havens to developing countries. These transactions facilitate a legalized form of money laundering which assists to wash the black money originated from developing countries to the same territory in the form of investment.

Tax Justice Network (TJN) has developed the Financial Secrecy Index (FSI), and this index ranks jurisdictions based on their secret and non-transparent financial activities (TJN 2018). This index gives an understanding of the financial secrecy, flow of capital, and illicit financial flow (TJN 2018). The world's most powerful countries, OECD members and their satellites are the major recipients of illicit flow through their offshore financial centres, and African countries' wealth has been stored in these centres by elites (TJN 2018).

Abovementioned examples clearly exhibit the enormous dimension of the problem. For brevity,

globalization enhances the capital flow across the world, but it also creates the chances to carry out money laundering in a legalized form through the tax havens, shell companies, and DTA treaties. Further, developing countries obtain this illicit money from offshore financial centres under the scheme of FDI with tax concessions.

Globally organized plunder: Do states require global solution through global governance to tackle money laundering?

Finally, I argue that money laundering requires global governance to be solved in an effective way, but strong regulations and good governance are the prerequisites at the domestic level.

From the above details, we can postulate that money laundering is a global problem and a global solution is inevitable in the globalized era to tackle this issue. How is global governance important and possible in this concern? The global policy on anti-money laundering in the globalized world has some unique problems.

Instead of relying on intergovernmental relationships, the global governance encompasses all comprehensive actors including local and international NGOs, citizens' movements, multinational cooperation, nation-states and global capital market (Weiss 2000, p.810). The policy of anti-money laundering also requires strong cooperation between financial professionals and law enforcement agencies across the world (Favarel-Garrigues, Godefroy & Lascoumes 2011, p.180). This cooperation results in tension between the state's sovereignty and neoliberal governmentality (Favarel-Garrigues, Godefroy & Lascoumes 2011, p.180). This is the main obstacle to achieve global cooperation in anti-money laundering problem. Effective global regulation of finance assists the supply of huge capital stock to the prosperity of humanity, and of marginalized groups of the world (Scholte 2011, p.110). But weak legitimacy is the common scenario of contemporary global governance (Z ?urn 2005; Buchanan & Keohane 2006 cited in Scholte 2011, p.111).

Financial Action Task Force (FATF) has established international standards to fight against money laundering. The article 37 of the FATF recommendations emphasize to provide strong mutual legal assistance between countries to combat money laundering (FATF 2018, p.25). But most recommendations insist on strong financial regulations through the competent authorities at the domestic level along with the sound international corporation. Despite the culture of confidentiality of banks in tax heavens, countries have achieved some outcome in the money laundering problem. In 2002 Organization for Economic Corporation and Development [OECD] released an agreement, and in 2015 OECD committee on fiscal affairs accredited to establish a protocol to form Tax Information Exchange Agreements (TIEA) among the nations through bilateral agreements to facilitate the exchange of information of persons who are suspected to involve in tax evasion practices (OECD 2019). Importantly, numerous offshore financial centres such as Virgin Island, Bahamas, Cayman Island, Switzerland, etc. have signed bilateral agreements with OECD countries (OECD 2019).

Notwithstanding, the efficacy of this agreement is questionable. The tax haven only corporate with countries for financial investigation when their submitted evidence is wrong (Addison 2009 cited in Sawyer 2011, p.44). Most TIEAs do not overrule the provisions of confidentiality of law of tax havens, and these TIEAs do not much underpin to curtail international tax cap (Avi-Yonah 2007 cited in Sawyer 2011, p.44). This situation degrades the overall purpose of TIEAs. The global governance on anti-money laundering reflects some empirical evidence to the realistic

views. International law's measures which prohibit anonymous participation in the global financial networks are ineffective, especially in G7 countries than tax havens (Sharman 2011. P.36). FATF publishes the blacklist of high-risked and monitored jurisdiction of having discrepancies of anti-money laundering practices (FATF 2019). Interestingly, the countries having higher financial secrecy index such as Switzerland, Hong Kong, Singapore, Panama, etc. (TJN 2018) have been carefully excluded from the FATF's list. Democratic governance is one of the main criteria for the legitimacy of global institutions, and multilateral institutions should make them more difficult for special interest's operations (Keohane 2011, p.103). But, TATF's actions exhibit realistic approaches of powerful countries in the global governance of the financial system. As Sharman (2011, p.1) mentioned, the powerful states impose international standards on other weaker states while they do not choose it to implement themselves.

Some improvements have been achieved in the global financial corporation. Recently, the Swiss government has signed with India to share the banking information of Indian depositors (Rupawat 2019). But, the central government of India refused to share the obtained information about black money under the Right to Information Act in the name of confidentiality of account holders (Scroll.in 2019). It is evident that countries should strengthen their national regulatory measures, and should develop a system of close collaboration for the information exchange (Reinicke 1998, p.158). Otherwise, money launders may use this disjuncture found between the internal legal system and nonterritorial character of global financial flow (Reinicke 1998, p.158). The Indian case is an example of the deficit of transparent governance of developing countries.

Developing countries have to adapt sound microeconomic policies and good governance through building up strong institutions and rules of law to reduce illicit financial flow (Kar 2011, p.54). It refers to the increasing power of the state to manage the money laundering problems, on the contrary to Friedman's prescriptions.

Due to its global nature, money laundering requires a global solution in long-run. But, at the present context, global governance of money laundering is intricate to implement since inefficiency of TIEA and less compliance of powerful states to international measures. Considering the developing countries, above Indian experience shows that transparency good governance and strong regulations are prerequisites to combat money laundering in an effective way since black money is formed within the territories.