

LEGAL BRIEFS

“FINCEN FILES” AND THE INVOLVEMENT OF INDIAN BANKS IN MONEY-LAUNDERING

NOTE-8/2020

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“FINCEN FILES” AND THE INVOLVEMENT OF INDIAN BANKS IN MONEY-LAUNDERING

Abstract

The FinCEN Files leak in 2020 exposed a vast network of suspicious financial transactions that were funneled through major global financial institutions, revealing the scale of money laundering, corruption, and financial misconduct that continues to plague the international banking system. This paper examines the involvement of Indian banks in these illicit activities, focusing on their role in facilitating the movement of illicit funds across borders. By analyzing the leaked documents, the study explores the methods employed by Indian financial institutions to conceal the origins and destinations of money flows, the loopholes in regulatory frameworks, and the regulatory failures that allowed such transactions to occur. Furthermore, it highlights the key vulnerabilities within the Indian banking system that may have been exploited for money laundering and other financial crimes. The paper also assesses the regulatory and policy measures taken by Indian authorities in response to the revelations, evaluating their effectiveness in curbing the prevalence of money laundering activities. Ultimately, the study calls for stronger compliance mechanisms, more stringent enforcement of anti-money laundering laws, and greater transparency in financial reporting to combat the growing threat of illicit financial flows in India and beyond.

Keywords: Regulatory Failures, Cross-Border Transactions, Indian Banks, Laundering Networks

Overview

On 20th September 2020 BuzzFeed News, in collaboration with the International Consortium of Investigative Journalists (ICIJ), published leaked documents recording unprecedented flows of laundered funds across the world. This tainted money was moved via formalized banking channels and used for terrorism and other illicit activities. The leaked documents include Suspicious Activity Reports (SARs) flagged by the US Department of Treasury's Financial Crimes Enforcement Network (FinCEN), detailing nearly \$2 trillion moved across 170 countries and territories between 2000-2017. Egregiously, 44 Indian Banks (both state and private owned) were also found involved in money laundering (and possible terror financing), totalling around \$1 billion in transactions that were flagged by the US Department of Treasury.

The purpose of this note broadly is to examine the impact of the FinCEN Leaks, particularly with regards to the global financial system. It will also contextualize the scope of Indian and Pakistani involvement recovered in the leaks, and identify ways, including legal and diplomatic recourses, available to move forward on the matter.

In light of the FinCEN Leaks,¹ this note explores the following questions:

- What is the FinCEN leak, and why did the global financial system fail to stop the flow of illicit monies?
- What are the possible implications of these leaks? Why are they important for Pakistan?
- What is the scope of Indian and Pakistani involvement in the FinCEN Leaks? Why should it matter?
- Finally, what steps can be taken by Pakistan to expose Indian involvement in money laundering and terrorism financing (ML/TF) as well as domestically improve its own capacity in addressing the same?

Introduction to FinCEN and the Global Financial System

The global regime on anti-money laundering and counter-terrorism financing (AML/CFT) requires countries to regulate financial sectors and channels to flag suspicious transactions as they arise. These suspicious transactions are then forwarded to Financial Intelligence Units (FIUs) for further analysis and may result in law enforcement investigations if warranted. The banking sector naturally serves as the cornerstone for compliance with the global AML/CFT regime and is tightly regulated by national and international supervisory mechanisms to ensure that suspicious financial behaviour is reported to FIUs for analysis. The ambit of suspicious activities in question range from insider trading, to ML/TF, and can be conducted by both individuals and firms. Banks are required to red-flag suspicious transactions by drafting Suspicious Transaction Reports (STRs) and sending these to FIUs for further investigation.

In the United States, the Treasury Department's Financial Crimes Enforcement Network (FinCEN) performs the role of an FIU and is tasked to combat financial crimes, including investigating US dollar transactions occurring outside the US. The suspicious transaction reports received by FinCEN are known as Suspicious Activity Reports (SARs).

The FinCEN leaks uncovered stories of financial fraud and money-laundering worth \$2 trillion² that took place between 2000-17 in over 170 countries and territories.³ Some of the leaked records were gathered as part of the US Congressional Committee's investigations into Russian interference in the 2016 US Presidential election.⁴ The ICIJ⁵ tracked down 18,153 transactions, with sending and beneficiary banking links established, totalling \$35 billion.⁶

The SARs⁷ in the FinCEN Files were mostly filed by a few large banks: Deutsche Bank (\$1.3 trillion), Bank of New York Mellon, Standard Chartered Bank, JP Morgan Chase (\$514 billion), Barclays and HSBC Bank; constituting over 85 per cent of all SARs in the leak.⁸

Major revelations include banks processing funds for individuals and companies involved in corruption, terror-financing, and drug trafficking. Most of these firms were already under the radar for terror-financing.⁹

It is important to note that the SARs in question are not proof or evidence of a violation of the law. They reflect concerns of potential malefaction with respect to certain transactions on behalf of banks, which are then communicated via SARs to governmental authorities for further analysis and investigation.

SARs are highly confidential, and cannot be accessed through ‘Freedom of Information’ requests nor court-orders. In the US, any unauthorized disclosure of a SAR makes an individual/entity liable for civil and criminal penalties. They can however be utilized as a ‘tip’ based on which further enquiries and formal investigations can be initiated by the relevant authorities.

Impact of the FinCEN Files

The FinCEN Files expose critical gaps in the global financial system. This differs from other leaks such as the Panama Papers based on the sheer scale of its activities and the emanating ML risk associated with it. The leaked documents involve not one or two companies, rather they extend to the entirety of the global financial system based on 170 jurisdictions. Moreover, the FinCEN Leaks barely represent 0.02% of the total SARs received by the authority since 2011,¹⁰ thus the potential scope and scale of TF/ML activities is likely to be far greater than anticipated.

In this context, the major question that arises is: post-FinCEN, what action can now be pursued by regulatory authorities to tackle and curb potential ML risks arising from such transactions?

Analysts believe that the revelations are unlikely to lead to additional regulatory penalties or fines, as banks have not broken any laws. At the basic level, the AML/CFT infrastructure in place at major financial institutions is operational, and reports are being filed as needed.

However, the leaks show that SARs are often filed months after the transaction has taken place, and the quality of the filed reports vary, especially when compared with the investigative action pursued against it.¹¹

The crucial loophole here is that banks are simply required to file a report with FinCEN. They are not required to terminate the suspicious activity or stop serving the suspect clients, as the documents are not substantial evidence of ML/TF and are legally shrouded in extreme confidentiality between the banks and the authorities. They do, however, expose the flaws of the banking system and the ineptitude of government authorities in countering them.

In terms of legal options, the US AML/CFT regime, governed by a range of laws, can be applicable since the transactions in question concern US banks, and so, fall within the ambit of US jurisdiction. FinCEN will have to go through the filed SARs and look into any irregularities. Due to the massive load of SARs already in the system (12 million from 2011-17 alone), this may take years. Once concrete evidence of ML/TF is found, the US legal regime is activated to prosecute the alleged launderers and financiers.

Given the scope of involvement of Indian entities and individuals – both within and outside of the US – it is pertinent to explore all such legal recourses available within the US AML/CFT legal framework. It is also important to understand the scope of both Indian and Pakistani involvement in the FinCEN Files when determining the nature of action to be taken. The following section summarizes these for both countries.

Scope of Involvement in ML/TF Activities

INDIA

A major revelation of the FinCEN leaks is the potential involvement of 44 Indian banks and financial institutions in suspicious transactions. The total transactions amounted to \$1 billion just during 2011-17 via 2,000 transactions,¹² flagged by major foreign banks like Deutsche Bank, Citibank, Standard Chartered, and JP Morgan Chase.¹³ Major Indian entities flagged ranged from potential antique smugglers, multinational conglomerates, to sponsors of the Indian Premier League (IPL) team.¹⁴ ANNEXURE III details some of these revelations.

The FINCEN Leaks successfully established sender-receiver connections for 406 transactions from the leaked files, involving major Indian banks, including the “Big Four” of India’s banking industry - State Bank of India, Punjab National Bank, ICICI Bank and HDFC Bank.¹⁵ (For the details of the number of transactions per involved bank, see ANNEXURE I and II).

Also included in these leaks are over 3000 transactions amounting to over \$1.5 billion related to Indian entities and individuals based in foreign jurisdictions.^{16,17}

Indian banks primarily figure in the SARs due to being "correspondent banks" to the foreign banks (not present in India) which have filed these SARs and figure in the network through which these transactions have been effected.¹⁸ Through correspondent banking relationships, banks can access financial services in different jurisdictions and provide cross-border payment services to their customers. This has become an arrangement over which there has been growing concern as regulators crack down on secrecy of offshore transactions. Records have shown cases where “suspicious transactions” have been carried out through the international payment gateway of foreign banks.¹⁹ In others, foreign branches of Indian banks such as a State Bank of India account in Canada and an account of Union Bank of India in UK have been used by clients for carrying out part of the transactions in question.

The FinCEN leaks have been largely met by silence in India both from government/regulators and the banking sector. Indian banking stocks, however, took a hit once the findings were published, fearing more bad news for the already stressed sector.²⁰ Some of the banks in question claim that the flagged transactions were already reported to the Reserve Bank of India (RBI) – India’s primary banking regulatory body – and investigations are already underway.²¹ However, most banks have refused to comment any further on the SARs, citing US confidentiality regulations.²²

From a legal perspective, the involvement of Indian Banks, especially the Punjab National Bank, in the FinCEN leaks is a significant development, especially since Pakistan’s recently released dossier on Indian efforts to destabilize Pakistan notes evidence of a \$28,000 transaction involving the “Punjab Bank India” from India to Afghanistan to fund terrorist activities against Pakistan.²³ Whether the FinCEN flagged transactions were further used to fund terrorism activities or otherwise contribute to terrorism financing is an important lawfare exercise which is explored in more detail below.

PAKISTAN

The FinCEN Files have also highlighted SARs involving Pakistani entities. While developing and pursuing lawfare strategies in this realm, it is important to analyze the scope of involvement of entities based in Pakistan and anticipate any legal challenges which this may cause for Pakistan.

The FinCEN Files show SARs issued against a Pakistani fertilizer company amounting to approx. \$3.8 million. Three other Pakistani companies²⁴ were also reportedly alleged for producing chemicals for suspicious activities.²⁵ Pakistani individuals have also been named in different SARs, including an owner of a food-related chain involved in a transaction of \$0.85 million.²⁶ Incidentally, Pakistan’s FIU, the Financial Monitoring Unit (FMU) was also alerted to the same, and an inquiry was commenced. The conclusion of this inquiry remains unknown.²⁷

A major revelation linked to Pakistan and India involved Altaf Khanani, a money launderer from Pakistan. Banks in India, Singapore and New York were found to have his money being processed.²⁸ Previously, Khanani's relationship with Dawood Ibrahim was documented by the US Office of Foreign Assets Control (OFAC) when it issued the sanctions notice against him after his arrest.²⁹ Khanani was apprehended at the Panama airport in September 2015, and it is unclear whether he has been deported to Pakistan or the UAE.³⁰

The OFAC, claiming movement of estimated \$14-16 billion annually, declared:

Altaf Khanani, the head of the Khanani MLO, and Al Zarooni Exchange to have been involved in dealings with the Taliban, Lashkar-e-Tayiba, Dawood Ibrahim, al-Qaida and Jaish-e-Mohammed.³¹

The FinCEN Leaks expose the extent of financial infiltration of Khanani's ML operation via a Dubai-based company and his dealings with a small New Delhi-based firm.³² Other companies associated to Khanani were also used for multiple transactions through Standard Chartered Bank and Deutsche Bank. The banks have not commented on the case.³³

From a legal perspective, this is a significant development, given the Indian efforts in demoting Pakistan to the Financial Action Task Force (FATF)'s list of 'High Risk Jurisdictions subject to a Call of Action' (or the 'black list'). Indian officials believe that the revelations about Khanani's operations in the FinCEN Files could strengthen their case against Pakistan.³⁴ Karnal Singh, a former director of Enforcement Directorate (an Indian law enforcement agency responsible for tackling economic and financial crimes) in an interview stated that this connection will "certainly help" India's case as it implicates Pakistan in not following UN [Security Council's] resolutions 1267 and 1373.³⁵ Whereas Graham Barrow, an anti-money laundering expert, told DW that "Khanani used a global network of shell companies, which means that it is unlikely that Pakistan will be dragged into it."³⁶

Way Forward and Suggested Actions

The India-Pakistan dynamic for many years has been hostage to sustained Indian attempts to portray Pakistan as a failing State, one that does not take its international responsibilities seriously and is complicit in promoting terrorism across borders. India's political and diplomatic offensive in this regard has been consistently supported by sophisticated media and lawfare maneuvers aimed at damaging Pakistan's reputation and international standing. The rise of the Modi-led BJP government propelled this policy into overdrive, aiming to diplomatically isolate Pakistan. However, in recent years, cracks have begun to appear in the Indian strategy due to increasingly brazen tactics³⁷ which expose India's mala fide intentions. At the same time, Pakistan has resolved to portray itself as a responsible state, dedicated to pursuing peace, economic stability and promoting regional trade and connectivity.

The prevailing environment thus provides Pakistan with a historic opportunity to reset its dynamic with India. International law in particular, can play a powerful role in guiding our foreign policy and domestic policy responses in this space. The FinCEN leaks provide interesting avenues for lawfare maneuvers which can be very useful in this regard.

Currently, Pakistan's lawfare options on this issue can broadly be classified as falling into two categories:

- Seeking greater international scrutiny of India for the Money Laundering/Terrorism Financing Risk emanating from its jurisdiction; and
- Pursuing liability for Indian banks by US authorities under US domestic law.

Seeking Greater International Scrutiny of India for the ML/TF Risk emanating from its jurisdiction

This objective requires focused and sustained engagement by Pakistan with a broad range of international organizations and standard setting/regulatory bodies on the ML/TF risk emanating from India. The objective would be to develop credibility and generate momentum for a fresh narrative, paving the way for formal engagement on this issue at the FATF and the Asia Pacific Group (APG). This will also require diplomatic lobbying with friendly states whose support would be required at multilateral forums. The following action points may be pursued from a legal perspective in pursuing this strategy:

- Detailed technical review by legal and financial integrity experts in Pakistan is required to identify the specific weaknesses in India's AML/CFT framework especially the failure of central banking services to detect and report transactions involving ML/TF risk, including by weak implementation of customer due diligence or internal controls and weaknesses in correspondent banking systems. This study should include the material contained in Pakistan's recent Dossier on Indian efforts to destabilize Pakistan.
- Based on the above, detailed memorandums must be prepared for various international organizations and standard setting/regulatory bodies drawing their attention, in line with their respective mandates, to the ML/TF risk emanating from India. Academic literature and seminars on this theme should also be conducted which are objective, technical and fact-based, engaging international AML/CFT experts.
- The APG is scheduled to conduct an on-site visit to India in February/March 2021 as part of its ongoing assessment of ML/TF compliance by states. Pakistan should closely monitor these developments and may provide nominated APG experts with legal memorandums detailing India's ML/TF risk and its adverse transnational impact.

- Similar memorandums may be prepared for FATF and APG member states who may be lobbied to nominate India for FATF-ICRG review.
- Actively pursue membership of the Egmont Group³⁸ (the international association of FIU's) now that all technical and legal requirements for its memberships have been met by Pakistan due to recent legislative amendments. Membership of the Egmont Group will enable Pakistan to establish intelligence-sharing ties between its Financial Monitoring Unit (FMU) and FinCEN along with 150 other FIU's around the world.
- Pak Missions in Australia (APG), Canada (Egmont Group), France (FATF), USA (IMF/World Bank) and Switzerland (Basel Committee for Banking Supervision) need to be provided with ongoing specialist technical and legal expertise so that they can effectively engage with international organizations and regulatory bodies in these countries and augment their diplomatic efforts in this area.

Since Pakistan is not a member of FATF and this is the first time that India would be targeted in the ML/TF realm internationally, immediate results should not be expected. Further, diplomatic maneuvers in this area should not be undertaken without careful planning otherwise they are likely to result in failure and undermine the credibility of Pakistan's narrative.

Since the Indian side is likely to focus on Pakistani persons and entities mentioned in the FinCEN leaks, it is important for Pakistan to timely investigate and if necessary, prosecute these individuals and entities under its new comprehensive AML/CFT framework. This will showcase the effectiveness of our legal and operational responses and demonstrate Pakistan's commitment to being a responsible state that takes its international obligations seriously. It will also help Pakistan in moving off the FATF 'grey-list'.

Sustained, institutional engagement by Pakistan in the AML/CFT realm will develop our understanding of the dynamics prevalent in this area and bolster the credibility of our narrative.

Pursuing Liability for Indian Banks by US Authorities under US Law

The FinCEN leaks also provide an opportunity to pursue legal liability of Indian banks under US law. As discussed above, a SAR does not by itself constitute evidence of wrongdoing but is merely information which is flagged for further analysis. The FinCEN leaks reveal that the SAR's involving Indian entities and individuals were mostly filed by major foreign banks (Deutsche Bank, Standard Chartered, JP Morgan Chase, Citibank etc.) who were in a correspondent banking relationship with Indian banks.

A key lawfare objective that can be pursued in this regard are penalties by US authorities on Indian banks involved in money laundering and potential terrorism financing which attract the application of US law. Some of the action points that can be pursued in this regard are as follows:

- In the case of the FinCEN leaks, the US Department of Treasury presumably already has jurisdiction since they have received SARs involving these banks. Simultaneously, Pakistan must seek to establish jurisdiction of the US Treasury & Justice Departments over the Indian banks involved in terrorism financing operations as set out in its November 2020 Dossier.
- Detailed research is required on the financial integrity of Indian banks mentioned in the FinCEN leaks and Pak Dossier including past transactions, reports of suspicious activity and details of regulatory compliance actions (if any) taken by the Central Bank of India, Reserve Bank of India and foreign jurisdictions against these banks. Follow-up actions taken by US agencies in response to the FinCEN reports must also be closely monitored.

- Based on the above, legal memorandums for relevant US authorities must be developed, highlighting specific violations of US law by Indian banks and requesting enforcement actions and the imposition of penalties against these entities.
- US law is highly technical in this subject and involves a maze of federal and state authorities. However, the strongest legal recourse against banks is provided by Section 311 of the USA PATRIOT Act, 2001 which allows the US Treasury Department to take “special measures” against foreign banks that do not adequately address ML/TF. These special measures include a range of options including penalties, sanctions and prohibitions on correspondent banking which provide the Treasury Department with a powerful and flexible regulatory tool to take actions to protect the U.S. financial system from specific threats.
- Pakistan’s November 2020 Dossier refers to ‘Punjab Bank India’ and provides evidence of its involvement in terrorism financing arrangements. If this bank actually is the Punjab National Bank referred to in the FinCEN files, then a powerful nexus is established of this bank’s involvement in terrorism financing triggering a wide range of enforcement actions and penalties under US law. This needs to be confirmed by the relevant authorities in Pakistan and pursued legally with US authorities.
- Simultaneously, similar memorandums can be prepared for friendly countries who are members of the Egmont Group with a request to share its contents with the Egmont Group and engage its review and compliance procedures.

The involvement of Indian banks in terrorism financing is perhaps the strongest component of Pakistan’s November 2020 Dossier. The FinCEN leaks potentially expose even bigger gaps in India’s financial institutions and have come at an opportune time. While actions against Indian state officials involving in money laundering and terrorism financing is likely to be blocked for political reasons, pursuing civil liabilities and penalties under US law for these banks is possible and would provide a big boost to Pakistan’s narrative and overall credibility.

However, as noted above, US law on this area is highly technical and exceedingly detailed. Any lawfare maneuvers in this field will have to be carefully planned after extensive research.

Annexure A

Bank Name ³⁹⁴⁰	Owned	Transactions Flagged
Punjab National Bank	State	290
Canara Bank	State	190
State Bank of India	State	102
Union Bank of India	State	99
Bank of Baroda	State	93
Bank of India	State	-
Indian Bank (Allahabad Bank)	State	-
Bank of Maharashtra	State	-
UCO Bank	State	-
Indian Overseas Bank	Public	-
Andhra Bank	Public	-
Vijaya Bank	Public	-
Standard Chartered Bank (India operations)	Foreign	-
Deutsche Bank (India operations)	Foreign	-
RBS	Foreign	-
Kotak Mahindra Bank	Private	268
HDFC Bank	Private	253
IndusInd Bank	Private	117
ICICI Bank	Private	57
Axis Bank	Private	41
YES Bank	Private	-
Karur Vysya Bank	Private	-
Tamilnad Mercantile Bank	Private	-
Karnataka Bank	Private	-

Annexure B

THE LIST

Top 5 receiver banks	No. of transactions	Received in \$ mn
Indian Overseas Bank	23	162.39
Allahabad Bank	26	144.24
Bank of India	35	130.76
State Bank of India	29	27.88
Canara Bank	37	3.31

Top 5 sender banks	No. of transactions	Sent in \$ mn
HDFC Bank	14	327.99
Deutsche Bank AG	18	53.76
IndusInd Bank	57	8.26
Standard Chartered Bank	1	8.17
State Bank of India	29	5.79

Source: ICIJ

Annexure C

Entities Involved (From)	Entities Involved (To)	Amount (millions)
HDFC Bank (11 transactions, 09/2012-02/2013)	Standard Chartered Bank	\$327.99
DBS Bank (19 transactions, Nov 2015-Apr 2016)	Bank of India	\$119.54
Deutsche Bank AG ⁴¹	Deutsche Bank ⁴²	\$53.52
Rak Bank (6 transactions, Mar 2014) ⁴³	SBI	\$23.32
A Seychelles-based Shell Company	A subsidiary of the Adani conglomerate (one of India's most powerful)	\$14.46
Rizal Commercial Banking Corporation (16 transactions, 01/2010-12/2010) ⁴⁴	Bank of India	\$11.21
IndusInd Bank (55 transactions, 06/2008-11/2012) ⁴⁵	HSBC	\$8.26
Standard Chartered Bank (1 transaction, 2011)	Merrill Lynch Bank Suisse	\$8.17
SBI (9 transactions, 01/2012-10/2012)	DNB ASA	\$5.79
Fraud case involving Indian Premier League (IPL) ⁴⁶		\$3
National Bank of Ras Al-Khaimah (20 transactions, 07/2013-11/2013)	Canara Bank (State-Owned)	\$2.76

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- ⁴⁵ The Business Standard (n 6)
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