Money Laundering Through the Ages: A Historical Analysis and Contemporary Regulatory Frameworks

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Abstract:

This paper delves into the evolution of money laundering practices from ancient times to the present day, tracing the historical roots of illicit financial activities. Beginning with early instances of currency debasement and smuggling, it examines the emergence of modern money laundering techniques alongside the development of banking systems. The analysis highlights key historical events and milestones that have shaped the landscape of financial crime, including the rise of organized crime syndicates and the globalization of illicit funds. Furthermore, the paper explores the evolution of regulatory frameworks and international efforts to combat money laundering, from the first anti-money laundering laws to contemporary regulations and enforcement mechanisms. By examining historical precedents and current trends, this study provides valuable insights into the ongoing challenges of detecting and preventing money laundering in an increasingly interconnected world.

Keywords: Money laundering, historical analysis, regulatory frameworks, financial crime, illicit funds, banking systems, organized crime, anti-money laundering laws, international efforts, enforcement mechanism

HISTORICAL BACKGROUND

The problem of money laundering has a long-standing historical foundation that spans many centuries. The beginnings of this phenomenon may be traced back to ancient times, during which individuals and organisations involved in criminal operations desired methods to obscure the sources of their unlawfully acquired profits. The phenomenon of money laundering has been more prominent in contemporary times due to the emergence of organised criminal activities, the establishment of worldwide financial networks,

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and improvements in the field of banking and finance. The operations of the Italian Mafia throughout the early 20th century represent one of the first known examples of money laundering. The Sicilian Mafia and other criminal organisations used various methods to launder profits generated from illicit operations including extortion, gambling, and drug trafficking. These methodologies included the use of front enterprises, shell corporations, and offshore accounts as means to obfuscate the trace of unlawful monies and incorporate them into the lawful economic system. The etymology of the phrase "money laundering" may be traced back to the mid-20th century, when it was used to describe the illicit transfer of funds by the Mafia via lawful enterprises. Nevertheless, it was not until the 1970s and 1980s that the issue of money laundering garnered substantial international recognition The occurrence of the Bank of Credit and Commerce International (BCCI) collapse in 1991 brought to light the extensive money laundering operations carried out by the bank, resulting in heightened examination and regulatory efforts aimed at addressing financial offences[3]. The perspective and strategy towards money laundering underwent a paradigm change in the 21st century. The events that occurred on September 11, 2001, brought attention to the connection between the funding of terrorism and the process of money laundering. As a result, countries and international organisations implemented more stringent measures to combat these dangers. The Financial Action Task Force (FATF), which was founded in 1989, has grown as a prominent global entity tasked with establishing benchmarks and advocating for efficient strategies to address the issues of money laundering and terrorism financing. The origins of money laundering rules in India may be traced back to the latter half of the 20th century. The need for comprehensive laws pertaining to anti-money laundering (AML) has become evident due to the increasing complexity of financial offences and the nation's expanding involvement in the global economic landscape. India's implementation of the Prevention of Money Laundering Act (PMLA) in 2002 was a notable achievement in its efforts to fight money laundering and conform to global norms. The ubiquitous nature of money laundering and the continuous development of tactics and strategies used by criminals to abuse financial institutions are underscored by its historical past. Furthermore, it underscores the significance of legislative frameworks, international collaboration, and technical progress in effectively tackling the complexities associated with money laundering in the present-day context. A comprehensive comprehension of the historical backdrop is important in order to assess the efficacy of India's regulatory structure and pinpoint potential avenues for enhancing efforts in addressing financial crimes.[4]

WHY MONEY IS LAUNDERED?

Money laundering is an intricate and diverse procedure that is propelled by a range of motivations and purposes. Gaining insight into the reasons behind money laundering is crucial for formulating efficient tactics to counteract this unlawful practice. The incidence of money laundering and its underlying reasons are influenced by several variables. Money laundering is primarily motivated by the desire to obscure the illicit origin of monies. Illicit revenues generated by criminal operations, including drug trafficking, human

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[3] https://www.investopedia.com/terms/a/aml.asp

smuggling, corruption, fraud, and organised crime, need the process of laundering in order to create the illusion of legitimacy. Through the process of money laundering, criminals may obfuscate the source of their income, so impeding law enforcement organisations' ability to track and confiscate illegal assets. Another primary incentive for money laundering is to avoid detection and prosecution by law enforcement. Financial intelligence units, regulatory bodies, and law enforcement organisations use laundering operations as a means to evade discovery by criminals. They use advanced methods like as strategizing transactions, using anonymous shell firms, and capitalising on regulatory gaps to impede authorities from uncovering their illegal operations. Money laundering is often used as a strategy to evade tax obligations and circumvent financial restrictions. Money laundering may be used by both individuals and businesses as a means to elude tax obligations, bypass currency restrictions, or conceal assets from regulatory examination. Offshore tax havens and intricate business structures are often used in money laundering operations with the aim of reducing tax obligations and preserving financial confidentiality.

Moreover, money laundering is intricately connected to the funding of terrorism and other unlawful endeavours. Terrorist entities and extremist factions depend on illicitly obtained monies to support their activities, acquire weaponry, enlist individuals, and carry out acts of aggression. Through the process of money laundering, these organisations are able to transfer monies over national boundaries, circumvent financial limitations, and covertly finance their operations. Moreover, money laundering functions as a catalyst for corruption and the unlawful movement of funds. Corrupt individuals, including officials, politicians, and businesspeople, engage in the practice of money laundering as a means to hide bribes, embezzled monies, and unlawful profits. Money laundering facilitates the flourishing of corrupt activities, weakens the effectiveness of government and openness, and diminishes public confidence in institutions. The underlying factors driving money laundering are intricately linked to the intricacies of the global financial landscape, improvements in technology, and the interdependence of financial institutions. The advent of the digital era has given rise to novel manifestations of money laundering, including cybercrime, virtual currencies, and online payment systems. Consequently, regulatory bodies and law enforcement organisations are confronted with supplementary complications.

To summarise, money laundering is motivated by a variety of linked factors, including the desire to hide illicit operations, elude discovery, dodge tax obligations, fund terrorists, enable corruption, and exploit weaknesses in financial systems. In order to effectively combat money laundering, it is imperative to adopt a comprehensive approach that encompasses several frameworks, including legal, regulatory, technical, and international cooperation measures. These measures should aim to disrupt and prevent money laundering operations.

MONEY LAUNDERING AND TAX EVASION

Money laundering and tax evasion are closely interconnected financial offences that often coincide, presenting substantial obstacles for regulatory bodies and law enforcement entities on a global scale. Gaining insight into the correlation between money laundering and tax evasion is essential for formulating

efficient tactics to fight financial offences and guarantee adherence to tax regulations[5]. Money laundering is the act of hiding the source of illegal money in order to make them seem lawful. Criminal enterprises, including drug trafficking, fraudulent operations, corruption, terrorism, and organised crime, provide significant financial gains that need the process of money laundering in order to evade discovery and legal consequences. The process of money laundering generally has three distinct phases, namely placement, layering, and integration. Illicit monies are brought into the financial system at the placement stage by cash deposits, wire transfers, or other methods. The layering step involves the execution of several transactions and transfers with the intention of concealing the origin of illegal monies. During the integration stage, the process involves the reintegration of laundered monies into the economy, whereby they are presented as apparently legal assets or investments. Tax evasion and financial fraud include the illicit practice of people or companies evading their tax obligations, often achieved by the underreporting of income, exaggeration of deductions, use of offshore 12 accounts, or involvement in other deceptive endeavours. Tax evasion has detrimental effects on governments by reducing their income, compromising the integrity of the tax system, and giving tax evaders an unfair advantage over taxpayers who comply with tax regulations. Financial fraud encompasses several forms such as accounting fraud, tax fraud, and false financial reporting. These fraudulent activities sometimes coincide with tax evasion and money laundering schemes, hence adding complexity to the identification and prosecution of financial crimes.

The dynamic relationship between money laundering and tax evasion:

There exists a strong correlation between money laundering and tax evasion, since both people and businesses may use various laundering methods to protect their income and assets from tax authorities. Proceeds obtained via money laundering may be used to cover expenditures, investments, and assets without arousing suspicion from tax authorities.

Typical techniques used for money laundering in relation to tax avoidance encompass: Individuals and corporations have the option to establish offshore accounts in countries that have advantageous tax regulations and banking confidentiality in order to conceal their income and assets from tax authorities. Offshore tax havens provide taxpayers with anonymity, little or nonexistent tax obligations, and lenient regulatory supervision, making them appealing to those who engage in tax evasion and money laundering. Money launderers and tax evaders often use shell firms, nominee directors, and intricate business structures to conceal the ownership and transfer of cash. These systems give rise to several levels of intricacy, hence posing difficulties for authorities in their efforts to track the movement of illegal monies and ascertain the eventual recipients. commercial-based money laundering refers to the act of manipulating international commercial transactions in order to transfer value and facilitate the movement of funds across national boundaries, all the while concealing the unlawful activities that underlie these operations. Trade-based laundering schemes and tax evasion are facilitated by the use of many techniques, including over- and under-invoicing, phantom shipments, and fraudulent documents. Laundered money might be allocated to real estate, luxury assets, and high-value commodities in order to conceal illegal riches and evade

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[5] https://www.fincen.gov/what-money-laundering

detection. Real estate transactions provide potential avenues for individuals engaged in money laundering and tax evasion to move substantial amounts of funds without arousing suspicion or necessitating reporting obligations. < Money launderers and tax evaders often use the assistance of experts, including attorneys, accountants, and financial consultants, to aid in the concealment of illicit activities, the organisation of transactions, and the exploitation of legal loopholes. Facilitators play a vital role in facilitating financial crimes and eluding identification by law enforcement agencies. [6]

The obstacles encountered in the fight against money laundering and tax evasion: Regulatory bodies, law enforcement agencies, and tax authorities face several hurdles in their efforts to combat money laundering and tax evasion. The aforementioned difficulties encompass: Transnational Nature: Money laundering and tax evasion are worldwide occurrences that transcend national boundaries, necessitating international collaboration and synchronisation to successfully tackle them. Illicit financial transactions spanning numerous nations are conducted by criminals who take advantage of jurisdictional variations, regulatory loopholes, and legal difficulties. The emergence of technological advancements, including cryptocurrencies, internet banking, and digital payment systems, has presented novel prospects and complexities for those engaged in money laundering and tax evasion. The use of digital currencies and anonymous transactions has the potential to enable criminal financial activity, hence posing challenges in terms of money traceability and monitoring . The detection and tracking of money laundering and tax evasion pose significant challenges due to the intricate nature of contemporary financial systems, including worldwide markets, investment vehicles, and financial instruments. The implementation of effective anti-money laundering (AML) and know-your customer (KYC) procedures pose obstacles for financial institutions, such as banks, in their efforts to prevent criminal activity. Regulatory compliance imposes duties on financial institutions and enterprises, including reporting requirements, due diligence processes, and risk assessments. The continuation of financial crimes may be attributed to many factors such as compliance costs, regulatory difficulties, and legal ambiguities, which may serve as incentives for particular businesses to engage in non-compliance or evasion. Resource constraints are a common challenge encountered by law enforcement organisations and tax authorities[7]. These limits include restricted finances, shortfalls in people, and flaws in technology. These limitations significantly affect their capacity to successfully investigate, punish, and discourage instances of money laundering and tax evasion. Implementation and Regulatory Actions: In order to effectively tackle the complexities associated with money laundering and tax evasion, governments and regulatory bodies use a range of enforcement and regulatory strategies, which encompass: The implementation and enforcement of Anti-Money Laundering (AML) laws, regulations, and directives are crucial in the prevention, detection, and prosecution of money laundering operations. Financial institutions are obligated by AML frameworks to do customer due diligence, report any suspicious transactions, and maintain strong compliance programmes. Enhancing tax compliance measures include bolstering procedures such as audits, investigations, fines, and reporting obligations. These measures aim to prevent tax evasion and encourage voluntary adherence to tax

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[6] https://www.investopedia.com/ask/answers/022015/what-methods-are-used-launder-money.asp

[7] https://www.napier.ai/knowledgehub/what-is-money-laundering

regulations. International cooperation plays a crucial role in bolstering efforts to fight cross-border money laundering and tax evasion by facilitating the exchange of information and collaboration across jurisdictions, financial intelligence units, law enforcement agencies, and tax authorities. Collaboration in detecting and prosecuting financial crimes is facilitated by international agreements, treaties, and partnerships.[8] Technological solutions include the use of advanced technologies, like data analytics, artificial intelligence, block chain, and machine learning, to augment financial transparency, boost risk assessment skills, and automate compliance operations. Technological interventions facilitate the identification of potentially illicit activity, the surveillance of financial transactions, and the recognition of recurring trends in money laundering and tax evasion. Public Awareness and Education: The objective is to enhance public consciousness about the ramifications of money laundering and tax evasion, foster ethical conduct, and provide people and companies with knowledge regarding their legal duties and obligations in addressing financial offences. This paper examines the regulatory framework and enforcement efforts in India. The regulatory framework in India pertaining to the prevention and mitigation of money laundering and tax evasion is regulated by a multitude of laws and regulatory agencies, which encompass Money Laundering Prevention Act (PMLA) The Prevention of Money Laundering Act (PMLA) is the main law in India that deals with money laundering. It establishes a legal structure for the prevention, detection, and punishment of money laundering crimes. The legislation requires the reporting of potentially illicit activities, established the financial information Unit-India (FIU-IND) as the primary entity responsible for receiving, analysing, and distributing financial information, and grants enforcement authorities the authority to seize and confiscate illicitly obtained funds. The Income Tax Act, in conjunction with other tax legislation and regulations, oversees the process of taxing and ensures adherence to tax rules.[9]

EXTENT OF MONEY LAUNDERING

The extent of money laundering globally is a complex and challenging phenomenon to quantify precisely due to its clandestine nature, cross-border transactions, and evolving methods employed by money launderers. However, various studies, reports, and assessments provide insights into the scale and impact of money laundering activities, highlighting the magnitude of the problem on a global scale. Estimates from reputable sources, including international organizations, financial institutions, and regulatory bodies, suggest that trillions of dollars are laundered globally each year. The International Monetary Fund (IMF) estimates that the value of money laundering transactions ranges from 2% to 5% of global GDP, amounting to hundreds of billions to trillions of dollars annually. These figures underscore the significant economic implications of money laundering and the challenges it poses to financial integrity and stability. The extent of money laundering is influenced by several factors, including the size of the global economy, the volume of financial transactions, the sophistication of criminal networks, and the effectiveness of regulatory and enforcement measures. Money laundering activities are prevalent in various sectors, including banking and

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[8] https://www.idnow.io/glossary/money-laundering/

[9]https://sanctionscanner.com/blog/money-laundering-and-tax-evasion-
80#:~:text=It%20is%20a%20deliberate%20act,hefty%20fines%20and%20even%20imprisonment

finance, real estate, trade, gaming, and professional services, reflecting the diverse avenues through which illicit funds are laundered. In India, the extent of money laundering is a growing concern, given the country's rapid economic growth, expanding financial sector, and increasing integration into the global economy. The Reserve Bank of India (RBI) and other regulatory authorities have highlighted the risks and vulnerabilities associated with money laundering, emphasizing the need for robust regulatory frameworks and proactive enforcement measures. The financial sector, including banks, non-banking financial institutions (NBFI), and payment systems, is particularly susceptible to money laundering activities due to the volume and complexity of financial transactions. Reports of money laundering scandals, financial frauds, and regulatory violations further underscore the challenges faced by financial institutions in detecting and preventing illicit activities. The real estate sector is another area of concern regarding money laundering, with reports of illicit funds being used to purchase high-value properties and assets. The lack of transparency in real estate transactions, coupled with the use of shell companies and nominee structures, creates opportunities for money launderers to conceal the true ownership and source of funds. Trade-based money laundering (TBML) is also a significant avenue for money laundering, involving the manipulation of international trade transactions to transfer value and move funds across borders. Over- and under-invoicing, false documentation, and misdeclaration of goods are common techniques used in TBML schemes, posing challenges for customs authorities and trade regulators. The extent of money laundering in India is further exacerbated by the nexus between money laundering, tax evasion, corruption, and illicit financial flows. High-profile cases of financial crimes, regulatory lapses, and enforcement challenges highlight the need for comprehensive anti-money laundering (AML) measures and enhanced international cooperation to combat illicit financial activities effectively. Efforts to assess the extent of money laundering in India include risk assessments, data analysis, suspicious transaction reporting, and collaboration with domestic and international partners. The Financial Intelligence Unit-India (FIU-IND) plays a crucial role in analysing financial intelligence, identifying money laundering trends, and supporting law enforcement agencies in investigating and prosecuting financial crimes. In conclusion, the extent of money laundering globally and in India reflects the pervasive nature of financial crimes, the vulnerabilities of financial systems, and the need for coordinated efforts to strengthen regulatory frameworks, enhance enforcement capabilities, and promote financial integrity. Understanding the scale and impact of money laundering is essential for developing targeted interventions, allocating resources effectively, and mitigating the risks posed by illicit financial activities.

IMPACT ON ECONOMY

Financial laundering has a significant and complex influence on the economy, including several aspects like as financial stability, market integrity, investor confidence, and overall economic growth. Money laundering presents substantial hazards and difficulties to both local and worldwide economies, compromising the credibility of financial systems and weakening public confidence in institutions. The distortion of financial markets and fair competition is a significant economic consequence associated with money laundering. Money launderers engage in the act of injecting unlawful monies into lawful economic

endeavours, hence establishing inequitable advantages for criminal firms in comparison to lawabiding businesses. The aforementioned distortion has the potential to result in market inefficiencies, pricing irregularities, and diminished competitiveness, hence adversely affecting lawful enterprises and investors. Money laundering plays a significant role in exacerbating economic instability via its facilitation of corruption, erosion of governance, and perpetuation of illegal financial transaction activities. The introduction of illicitly obtained cash into the economy has the potential to disrupt investment trends, artificially inflate the value of assets, and generate speculative bubbles within the real estate and banking sectors. The presence of these distortions has the potential to result in economic imbalances, asset bubbles, and systemic hazards, hence presenting significant dangers to both financial stability and macroeconomic resilience. Furthermore, the act of money laundering has a detrimental impact on investor confidence and gradually diminishes trust in both financial institutions and markets. The idea of pervasive money laundering and financial crime has the potential to dissuade both local and international investors, impede the entry of capital, and restrict chances for economic progress. Jurisdictions characterised by inadequate anti-money laundering (AML) measures may be seen by investors as posing a higher level of risk and instability, hence resulting in capital flight and diminished inflows of investment. Money laundering has a detrimental effect on several sectors of the economy, including banking, finance, real estate, commerce, and professional services. Money laundering scandals and compliance breaches expose financial companies to reputational hazards, regulatory punishment, and financial losses. Anonymity and opacity in real estate transactions may lead to distortions in property values, speculative bubbles, and heightened risks of money laundering in the industry.

TBML, or trade-based money laundering, has the potential to disrupt global trade patterns, improperly distribute resources, and compromise the integrity of trade. Trade data may be distorted, tariff revenues can be affected, and illegal actors might gain unfair trade benefits due to over- and under-invoicing, misdeclaration of items, and trade-based schemes. The detection and prevention of illegal trade operations are also posed issues for customs officials, trade regulators, and supply chain actors in the context of TBML. Furthermore, money laundering has wide-ranging social and environmental consequences, such as enabling organised criminal activities, financing acts of terrorism, continuing the issue of human trafficking, and intensifying environmental offences. Laundered monies have the potential to be used for the purpose of funding illicit operations that inflict damage upon communities, exploit people who are vulnerable, and destroy natural resources. The interconnections between money laundering and other criminal activities underscore the interdependence of financial offences and their detrimental impacts on both society and the environment. The economic ramifications of money laundering in India are a matter of considerable importance, considering the nation's economic expansion, advancement in the financial sector, and incorporation into international markets. The significance of addressing money laundering has been underscored by the Reserve Bank of India (RBI) and other regulatory bodies in order to maintain financial stability, preserve market integrity, and foster investor trust. Initiatives aimed at alleviating the economic ramifications of money laundering include the reinforcement of anti-money laundering (AML) rules, the augmentation of financial transparency, the advocacy for ethical corporate conduct, and the cultivation of
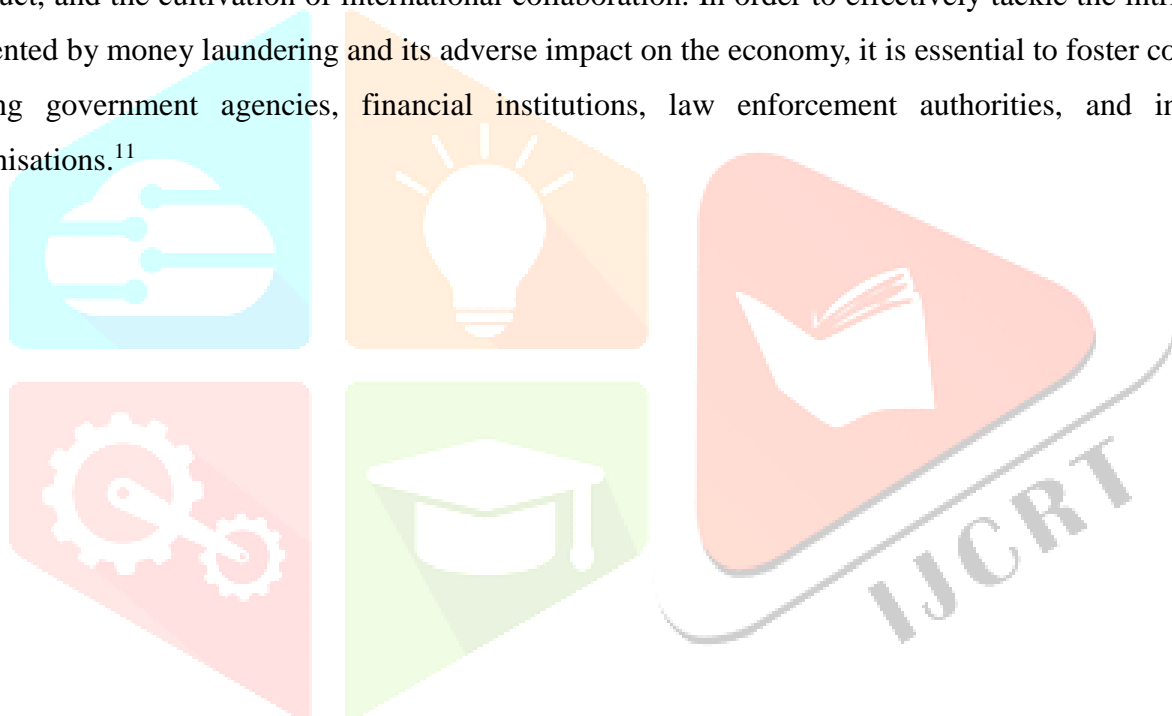
international collaboration. In order to effectively tackle the intricate issues presented by money laundering and its adverse impact on the economy, it is essential to foster collaboration among government agencies, financial institutions, law enforcement authorities, and international organisations.[10]

COMBATING OF THREAT

Financial laundering has a significant and complex influence on the economy, including several aspects like as financial stability, market integrity, investor confidence, and overall economic growth. Money laundering presents substantial hazards and difficulties to both local and worldwide economies, compromising the credibility of financial systems and weakening public confidence in institutions. The distortion of financial markets and fair competition is a significant economic consequence associated with money laundering. Money launderers engage in the act of injecting unlawful monies into lawful economic endeavours, hence establishing inequitable advantages for criminal firms in comparison to lawabiding businesses. The aforementioned distortion has the potential to result in market inefficiencies, pricing irregularities, and diminished competitiveness, hence adversely affecting lawful enterprises and investors. Money laundering plays a significant role in exacerbating economic instability via its facilitation of corruption, erosion of governance, and perpetuation of illegal financial transaction activities. The introduction of illicitly obtained cash into the economy has the potential to disrupt investment trends, artificially inflate the value of assets, and generate speculative bubbles within the real estate and banking sectors. The presence of these distortions has the potential to result in economic imbalances, asset bubblesand systemic hazards, hence presenting significant dangers to both financial stability and macroeconomic resilience. Furthermore, the act of money laundering has a detrimental impact on investor confidence and gradually diminishes trust in both financial institutions and markets. The idea of pervasive money laundering and financial crime has the potential to dissuade both local and international investors, impede the entry of capital, and restrict chances for economic progress. Jurisdictions characterised by inadequate anti-money laundering (AML) measures may be seen by investors as posing a higher level of risk and instability, hence resulting in capital flight and diminished inflows of investment. Money laundering has a detrimental effect on several sectors of the economy, including banking, finance, real estate, commerce, and professional services. Money laundering scandals and compliance breaches expose financial companies to reputational hazards, regulatory punishment, and financial losses. Anonymity and opacity in real estate transactions may lead to distortions in property values, speculative bubbles, and heightened risks of money laundering in the industry. TBML, or trade-based money laundering, has the potential to disrupt global trade patterns, improperly distribute resources, and compromise the integrity of trade. Trade data may be distorted, tariff revenues can be affected, and illegal actors might gain unfair trade benefits due to over- and under-invoicing, misdeclaration of items, and trade-based schemes. The detection and prevention of illegal trade operations are also posed issues for customs officials, trade regulators, and supply chain actors in the context of TBML. Furthermore, money laundering has wide-ranging social and environmental consequences, such as enabling organised criminal activities, financing acts of terrorism,

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[10] https://sanctionscanner.com/knowledge-base/trade-based-money-laundering-tbml-40

continuing the issue of human trafficking, and intensifying environmental offences. Laundered monies have the potential to be used for the purpose of funding illicit operations that inflict damage upon communities, exploit people who are vulnerable, and destroy natural resources. The interconnections between money laundering and other criminal activities underscore the interdependence of financial offences and their detrimental impacts on both society and the environment. The economic ramifications of money laundering in India are a matter of considerable importance, considering the nation's economic expansion, advancement in the financial sector, and incorporation into international markets. The significance of addressing money laundering has been underscored by the -on-anti-money-laundering-and-combating-financing-of-terrorism- Reserve Bank of India (RBI) and other regulatory bodies in order to maintain financial stability, preserve market integrity, and foster investor trust . Initiatives aimed at alleviating the economic ramifications of money laundering include the reinforcement of anti-money laundering (AML) rules, the augmentation of financial transparency, the advocacy for ethical corporate conduct, and the cultivation of international collaboration. In order to effectively tackle the intricate issues presented by money laundering and its adverse impact on the economy, it is essential to foster collaboration among government agencies, financial institutions, law enforcement authorities, and international organisations.[11]

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[11]https://www.ricago.com/blog/laws-on-anti-money-laundering-and-combating-financing-of-terrorism-in-india#:~:text=The%20primary%20legislation%20governing%20anti,for%20AML%20in%20the%20country.