

India's Currency Reform Already Paying Dividends in Fight Against Terrorism: Analyst

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In a Nov. 8 televised address, India's Prime Minister Narendra Modi told the nation of his decision to withdraw 500- and 1,000-rupee banknotes from circulation as part of the country's broader crackdown on financial crime. The notes no longer constituted legal tender as of midnight that night.

In some respects the policy has already paid off, according to Amit Kumar, a terrorist financing analyst in Washington, D.C. and president of AAA International Security Consultants LLC. Early reports indicate that blacklisted militant groups have found it much more difficult to raise and move funds in the country.

But "demonetization" is just one of several recent government initiatives to force India's sprawling, informal, cash-based economy to the surface and impose more transparency on digital payment systems, and should be seen in that context, Kumar said in a recent interview with ACAMS [moneylaundering.com](#) reporter Valentina Pasquali.

What follows is an edited transcript of their conversation.

How has India's currency reform progressed thus far?

Holders of the retired notes were given until the end of the year to exchange them for revamped 500-rupee notes, or newly minted 2,000-rupee notes the government would roll out in line with its decision. Alternatively, authorized accountholders were permitted to deposit them at their banks after showing the required identification in accordance with India's increasingly thorough know-your-customer requirements.

Overall, the 500- and 1,000-rupee notes that would be retired comprised nearly 86 percent of all notes in circulation at that time, with a total value of some \$220 billion.

"Remonetization" is ongoing. The Reserve Bank of India said recently that about 60 percent of the withdrawn notes have already been replaced with the new 500- and 2,000-notes. By most accounts this process is on pace to be largely completed by end of February.

What did the prime minister set out to accomplish with this decision?

His reasons were manifold, but this was only the latest in a series of actions he and his government have taken since coming to power in May 2014. They pushed a black money law through Parliament in 2015, then passed a beneficial ownership law and a goods and services tax law in 2016. So this currency reform is not a standalone initiative and must be read in that context.

The overall goal is to attack corruption, terrorist financing and untaxed wealth outside the licit economy. It is geared toward bringing more transparency to the system while also increasing tax revenues, financial inclusion and social justice.

The government has also taken steps to encourage individuals that never had a bank account to open one. The hope is that banking the unbanked and regulating the unregulated will ultimately fuel economic growth, even if liquidity is drained in the short term.

Could you tell us a little more about the black money and beneficial ownership laws you mentioned?

The black money law was aimed at forcing Indians who had stashed their wealth abroad, for example in Swiss banks, to reveal those assets, declare them to the authorities and pay some penalties. This money could then go back into the licit economy and be regularly tracked by the government and law enforcement.

The beneficial ownership law targets wealthy people who own real estate under a proxy's name. It's a complex piece of legislation, but basically it enables investigations into who the real, beneficial owners of property in India are and gives authorities power to prosecute them and confiscate their holdings when warranted.

Returning to currency reform: what have been the effects of this policy thus far on illicit financial flows?

On the terrorist-financing front the results have been very positive. Government sources and data tell us that there's been a reduction in activity, including across the fake Indian currency market that is often used to fund terror groups.

One piece of data says there's been a 60 percent dip in terror-related activities and a 50 percent reduction in terror-related hawala transactions being funded from across the border in Pakistan. Additionally, at least two presses in Pakistan that were printing fake Indian currency notes and pumping them into India were forced to shut down.

More tax evaders have been brought under the scanner, though there isn't any data yet on the volume of black money that has been flagged because it is still too soon after demonetization was initiated.

The Indian finance minister also announced that both direct and indirect tax revenue has increased as a result of demonetization and so will the tax base.

Increasing digital payment activity through mobile banking and other platforms was also one of the goals of demonetization. The government of India is taking the lead on this and it has created a mobile payment system of its own, where it encourages bank account holders to make secure online payment transactions through their mobile phones. That system, which is called BHIM, was launched at the end of the demonetization period. All these developments are making the Indian fintech sector attractive for both foreign and domestic investors.

What do you make of criticism that the policy was announced and carried out too suddenly?

Things were kept under the radar and only a few officials beyond the prime minister knew about it to prevent leaks. Had word gotten out, tax evaders, financial criminals and terrorist financiers would have had the opportunity to eliminate their illicit cash holdings or convert them into other assets. So the surprise element was critical. As a result there has been some economic discomfort, but whenever you have what I would call a necessary disruption there is bound to be some of that.

What else do you think the government has in store to crack down on illicit finance?

One of the complaints that domestic and foreign investors have about India is corruption, and the prime minister has pledged to attack it. This coming year will also see the implementation of the goods and services tax to rationalize the indirect tax system in India. That's a big thing. The rollout starts in July and will hopefully result in increased tax efficiency and overall tax compliance.