THE INVISIBLE BANK: REGULATING THE HAWALA SYSTEM IN INDIA, PAKISTAN AND THE UNITED ARAB EMIRATES

Adil Anwar Daudi

INTRODUCTION

In the labyrinthine depths of old Delhi, where the lanes are too narrow even for a rickshaw, men drink tea and chat in shabby offices. Nobody seems to be doing any work, until the phone rings. Then, numbers are furiously scribbled, followed by some busy dialing and whispered instruction. Although it’s far from obvious in the innocuous setting, these men are moving money – to exporters, drug traffickers, tax evaders, corrupt politicians. And terrorists.

In October 2001, nearly one month after the September 11, 2001 terrorist attacks, Time Magazine published an article entitled “A Banking System Built for Terrorism” which led with the paragraph quoted above. The “sinister picture” depicted by the Time Magazine author is of a hawala transaction, an ancient, and until now, virtually unregulated informal funds transfer (IFT) system that has drawn severe criticism for its susceptibility to abuse by terrorists and other criminal elements. Indeed, descriptions of hawala, like that illustrated by the Time Magazine author, portray it to be a peculiar financial

1. Doctor of Jurisprudence 2005 (expected), Indiana University School of Law – Indianapolis. Bachelor of Arts in Political Science and Economics 2002, University of Michigan – Ann Arbor. The author would like to recognize his parents, Dr. Anwar Daudi and Rafat Daudi, for their sacrifice and commitment to helping all their children reach their highest potential.


3. See MOHAMMED EL QORCHI ET AL., INTERNATIONAL MONETARY FUND, INFORMAL FUNDS TRANSFER SYSTEMS: AN ANALYSIS OF THE INFORMAL HAWALA SYSTEM 6 (2003). There are four reasons why the term IFT is used to describe hawala type transactions: First, in some jurisdictions, these systems are the dominant means by which financial transfers are conducted and therefore cannot be referred to as “alternative remittance systems.” Second, in some communities, informal funds transfer service providers operate openly – with or without government recognition; thus, this system cannot be referred to as “underground.” Third, the use of these mechanisms is often cross-cultural and multiethnic; thus the term “ethnic banking” is overly restrictive. Fourth, IFT better captures the sense and nature of financial transfers akin to conventional banking that are of primary interest. . . .

Id.
system that is both dangerous and beyond ordinary analysis. References to the hawala system have become ambiguous over time and consequently invoke a combination of confusing and sometimes conflicting images. The hawala system is often discussed in an alleged connection with money laundering, terrorist activities, or as a mysterious system for “moving money without money moving at all, and without leaving traces or records.” Contrary to these portrayals John F. Wilson, a senior economist with the International Monetary Fund (IMF), argues that hawala should be understood as an “economic phenomenon,” comparable in mechanics and economic structure to most remittance alternatives, which can only be regulated by reducing the economic incentives to engage in hawala.

The September 11 terrorist attacks against the United States shifted media attention to IFT systems like hawala and their alleged connection to money laundering and terrorist activities. This has increased the level of concern about IFT systems’ susceptibility to financial abuse from entities like the IMF, the World Bank Group (World Bank), and the Organisation for Economic Co-operation and Development (OECD). Two years after the attacks, the international community is still attempting to locate and strengthen gaps and weaknesses in legal and financial systems worldwide. The impetus of this global effort to regulate IFT systems, particularly hawala, has stemmed from measures recommended by the Financial Action Task Force on Money

4. Id.
6. Id.
7. Wilson, supra note 5, at 12; see also International Monetary Fund, About the IMF, at http://www.imf.org/external/about.htm (n.d.) (last visited Mar. 24, 2005). “The IMF is an international organization of 184 member countries. Since the IMF was established its purposes have remained unchanged but its operations – which involve surveillance, financial assistance, and technical assistance -- have developed to meet the changing needs of its member countries in an evolving world economy.” Id.
10. Morais, supra note 8, at 1.
Laundering (FATF). However, international guidelines designed to bring hawala under a regulatory umbrella fail to account for the reasons why hawala has survived for so many years and why it is likely to continue to survive despite increased regulation.

This note will detail the mechanics behind the hawala informal funds transfer system and evaluate its operation and potential for long-term existence against new international guidelines designed to regulate hawala businesses. This note will expand arguments advanced by Wilson and other IMF economists and suggest that, beyond formal financial sector reforms, the political environment in countries seeking to regulate their hawala markets should be given equal weight. To this end, this note will analyze and discuss the merits of three different models of domestic regulation of the hawala system, in India, Pakistan, and the United Arab Emirates (UAE), which have been modeled after international recommendations and are designed to police hawala transactions.

The discussion is broken into three parts. Part One will focus on hawala transactions generally. Part One summarizes the findings of a joint study conducted by the IMF and the World Bank regarding the mechanics behind a typical hawala transaction. This section chronicles the history of the hawala system by considering several characteristics of hawala transactions that help explain the reasons behind its development and why it continues to be an appealing transfer system today. Additionally, this section will outline IMF and World Bank studies that link the hawala system to both legitimate and illegitimate activities, which has caused its existence to raise concern in the international community. Part Two will outline the legislation that has emerged to check hawala businesses and transactions, primarily by examining the strength of international regulations sponsored by FATF. Finally, Part Three studies the merits of domestic regulatory efforts against hawala businesses in India, Pakistan, and the United Arab Emirates (UAE), which have been designed to regulate the hawala system and assess the relative success and failure of these legislative efforts.

11. See The Financial Action Task Force On Money Laundering, OECD, History of the FATF, at http://www1.oecd.org/fatf/AboutFATF_en.htm#History (n.d.) (last visited Feb. 28, 2005). "In response to mounting concern over money laundering, the Financial Action Task Force on Money Laundering (FATF) was established by the G-7 Summit that was held in Paris in 1989. . . . The G-7 Heads of State or Government and President of the European Commission convened the Task Force from the G-7 member States, the European Commission, and eight other countries." Id.
PART ONE: HAWALA

A. Contemporary Mechanics of Hawala

The modern hawala system, which has not derogated from its roots, works by transferring funds outside of "or parallel to 'traditional' banking or financial channels."12 A typical transaction can be described as follows:

A remittance from a customer (CA) from country A, or a payment arising from some prior obligation, to another customer (CB) in country B. [Where] a hawaladar from country A (HA) receives funds in one currency from CA and, in return, gives CA a code for authentication purposes. He then instructs his country B correspondent (HB) to deliver an equivalent amount in the local currency to a designated beneficiary (CB), who needs to disclose the code to receive the funds. HA can be remunerated by charging a fee or through an exchange rate spread. After the remittance, HA has a liability to HB, and the settlement of their positions is made by various means, either financial or goods and services. Their positions can also be transferred to other intermediaries, who can assume and consolidate the initial positions and settle at wholesale or multilateral levels.13

Interpol14 and IMF economists have identified three general principles represented in this typical hawala transfer that help to explain the mechanics behind the system and aid in establishing a broad definitional framework from which to draw upon. First, most hawala transactions involve simple trust relationships between hawaldars allowing transactions to cross international lines.15 Second, the hawala system, at least implicitly, involves more than one currency.16 Finally, hawala transactions involve settlement mechanisms through principles and intermediaries.17

14. Interpol, Vision, at http://www.interpol.com/Public/Icpo/default.asp (n.d.) (last visited Feb. 27, 2005). "Interpol exists to help create a safer world. Its aim is to provide a unique range of essential services for the law enforcement community to optimi[z]e the international effort to combat crime." Id.
15. Wilson, supra note 5, at 2.
16. Id.
17. Id. See also QORCHI ET AL., supra note 3, at 14.
1. Trust and International Hawala Transactions

In the simple international hawala transaction detailed above, the first, and arguably most important, element of a hawala transaction is embodied: trust. There are two prongs to the trust relationship in this classic hawala transaction that require attention. First, there is a trust relationship between the hawaladar in country A (HA) and his or her customer in country A (CA). Second, there is trust relationship between HA and the hawaldar in country B (HB). Note that in the transaction described above, there is no exchange of receipts between HA and CA. Moreover, HA's recordkeeping is designed to account for the total money that is owed to HB instead of recording individual remittances he or she has made. A violation of either of these trust relationships between hawaladars is described as an "economic death sentence" punished by ex-communication and "loss of honour."

2. More Than One Currency

A hawala transaction is likely to involve two currencies with no participant in the transfer purchasing or selling any one currency on the foreign exchange market. These transactions are accomplished "on a large scale and on-going basis" through a familial network or other connections among
Independent studies by IMF and Interpol have identified several possible ways in which these networks can be formed that indicate the implicit foreign currency exchange process that is present in each *hawala* transaction. The first possibility is that HA and HB are business partners where "for them transferring money is a part of another business in which they are engaged but still part of their normal business dealings with one another." Another possibility is that HB may owe a debt to HA, and due to difficulties in moving money out of HB's home country, HB can repay his or her debt to HA by paying HA's *hawala* customers. A final possibility is that HA has a surplus of currency in HB's country, and HB is helping HA to dispose of it. Note that in the final two scenarios there is neither an exchange of currency nor does HB need to recover any money; HB is either repaying an existing debt to HA, or handling money that HA has entrusted to HB.

3. Settlement Procedures

The claim that *hawala* "sends money without sending money" is deceptive. These types of claims often stem from recognizing that the settlement aspects of informal *hawala* transactions are obscure. Despite this acknowledgment, IMF and World Bank economists studying the *hawala* system have defined various settlement designs behind a typical *hawala* transaction that help illustrate the mechanics behind *hawala*. These settlement arrangements range from: (1) reverse transactions; to (2) bilateral settlement arrangements.

The most obvious form of settlement for *hawala* accounts is "reverse *hawala*" or a "remittance and payment going in the opposite direction through the same two *hawaladars*." The likelihood of account balancing through "reverse *hawala*" is small because of the "low probability that *hawala* remittances from country B to country A would pass through the same
Also, because aggregate remittance flows are unbalanced, with some countries acting as natural net sources of remittances and others carrying large outflows of private transfers, it would seem "mathematically difficult for a significant fraction of hawala activity to be 'settled' through simple or bilateral reverse transactions."\(^{36}\)

The more likely debt settlement procedure is one involving bilateral financial settlement using third country accounts.\(^{37}\) Under this rubric, HA can settle obligations to HB through a deposit in an account maintained by HB, which is located in a country that readily accepts convertible currency transactions.\(^{38}\) In this model, no actual foreign exchange transaction has taken place between HA and HB as the underlying exchange rate is implicit in the relationship between the hawala remittance and the settlement account.\(^{39}\)

B. Roots of the Hawala System

1. Hawala and Formal Transfer Systems

Informal funds transfer (IFT) systems have been in use in numerous regions around the world for many years.\(^{40}\) The hawala system is a type of IFT system that exists under many names and in many countries of the world.\(^{41}\) The hawala system is one of the earliest banking systems in history, predating even "traditional" or "western" banking.\(^{42}\) Hawala developed in South Asia and was used primarily for trade financing.\(^{43}\) The dangers of traveling with gold and

\(^{35}\) Id.
\(^{36}\) Id.
\(^{37}\) Id. at 15.
\(^{38}\) Id.
\(^{39}\) Id.

40. EL-QORCHI, supra note 13. Mohammed El Qorchi a senior economist with the IMF, has chronicled the history of the hawala system and indicates in this article that IFT systems are used in many regions around the world for transferring funds, both domestically and internationally. See also JOST & SANDHU, supra note 12 (discussing hawala's status as a major remittance system used around the world). For a discussion on other IFT systems in Asia and South America, see Morais, supra note 8, at 1.

41. EL-QORCHI, supra note 13; see also Report on Money Laundering Typologies, FATF, Doc. FATF-XIV 3 (Feb. 14, 2003) (describing different variations of the hawala system including hundi, fei-chen and the black-market peso exchange).

42. JOST & SANDHU, supra note 12 (discussing hawala's origins in India before the introduction of western banking practices). For a discussion on early Islamic Banking and the initial development of promissory notes, assignments and transfer of debts via bills of exchange by Muslim merchants, see Vaknin, supra note 23.

43. JOST & SANDHU, supra note 12. Consider the following narrative of an early hawala transaction where:

In 1424 by the Christian calendar, Rashid Ibn Umar al-Muza contemplated the dangerous journey he was about to begin. His trading caravan had met with great success (Allah be praised) and now, in Begram in the Kushan Empire, camels laden with art, furs and spices, Rashid was ready to set off. In his satchel he carries his caravan's profit as marks on a sheepskin. Rashid repatriated his
other forms of payment on routes plagued with thieves and bandits necessitated its development. The term hawala means "transfer" or "wire" in Arabic and is distinguished from the "hawala system," which "refers to an informal channel for transferring funds from one location to another through service providers — known as hawaldars — regardless of the nature of the transaction and the countries involved." The spirit of a hawala transfer is informality. The remittance occurs from one party to another without the use of a formal financial institution like a bank or money exchange.

Media and even academic comments on informal transfer systems like hawala note that "[they] can be used to send money without sending money." These portrayals suggest that hawala transfers are something different from more institutionalized means of making international payments. In comparing contemporary conventional remittance channels, such as banks and exchange houses, including facilities like Western Union and MoneyGram, it is apparent that the mechanics of such transactions are strikingly similar to the hawala system. Under both the hawala system, and formal remittance

earnings by Hawala, an ancient form of money transfer. For added safety, only Rashid knew the secret greeting that would validate his sheepskin. Rashid repatriated his earnings by Hawala . . .


44. JOSEPH & SANDHU, supra note 12; see also Vaknin, supra note 23 (describing hawala as a system older than the West). For a discussion on hawala as a traditional method of moving money in South Asia in order to protect early merchants against robbery on the silk road, see BEATE REZAT, HAMBURG INSTITUTE OF INTERNATIONAL ECONOMICS, HAWALA, at http://www.hwwa.de/Projekte/luD_Schwerpunkte/IDSPs/Asia_Gateway/Hawala.htm (n.d.) (last visited Feb. 2, 2005).

45. EL-QORCHI, supra note 13; see also Looney, supra note 18 (defining hawala as a transfer or remittance from one party to another); REZAT, supra note 44 (defining hawala as an “ unofficial alternative remittance and money exchange system enabling the transfer of funds without their actual physical move.”); Senator Evan Bayh, Prepared Statement at the Hearing Before the Subcommittee on International Trade and Finance on Hawala and Underground Terrorist Financing Mechanisms (Nov. 14, 2001) (on file with author) [hereinafter Congressional Hearing] (describing hawala to consist of “system brokers that provid[e] paperless banking transactions and enables individuals to transfer large sums of cash from one country to another without the funds ever crossing borders or being recorded.”); Report on Money Laundering Typologies, FATF, Doc. FATF-XIV 3 (Feb. 14, 2003) (distinguishing between the Arabic term “hawala” and the “hawala information transfer system”).

46. Looney, supra note 18. The Hawala system in conventional definitions is simply a transfer or remittance from one party to another, “without the use of a formal financial institution such as a bank or money exchange, and is in this sense an ‘informal’ transaction.” Wilson, supra note 5, at 2.

47. Id. at 1.

48. Id.

49. MANUEL OROZCO, MULTILATERAL INVESTMENT FUND OF THE INTER-AMERICAN DEVELOPMENT BANK, WORKING PAPER ON WORKER REMITTANCES IN AN INTERNATIONAL SCOPE 6 (March 2003). Western Union has the largest worldwide presence in the money transfer industry with one-quarter of the global market. Id.

50. Id. “Companies like MoneyGram and Thomas Cook also operate globally, though with a lesser presence than Western Union.” Id.

51. Wilson, supra note 5, at 5.
channels, "payments are made out of balances at the receiving end, with settlements to follow or, in cases where there are no exchange control issues, institutional accounts can be debited/credited congruently."52 Indeed, Wilson is accurate in his suggestion that from an economic and accounting perspective there are very few dissimilar models of remittances systems around the world with the main difference being their respective relationship to institutional or informal financial channels.53

2. Why Hawala?

The hawala system's apparent likeness to more common remittance systems begs the question – why would individuals continue to use the less formal hawala system in lieu of more institutionalized financial remittance systems? A joint study by the IMF and World Bank, in addition to an independent examination conducted by Interpol, advance several motivations behind the modern day use of the hawala system, including the: (1) cost effectiveness;54 (2) speed,55 and (3) versatility of each transaction.56

One of the primary reasons behind why hawala competes effectively with other remittance mechanisms is due to its cost effectiveness.57 Hawaladars are remunerated by charging a fee for each transaction and are often able to keep their expenses lower than payments made through the formal banking sector.58 The lower expenses maintained by hawaldars can be explained by examining the infrastructure required by hawala dealers to carry out business activities, which is less complicated compared to that of banks involved in international payment transactions or even international money changers.59 Indeed, hawaladars are capable of operating from "their homes or little shops, or can be accommodated within already existing businesses[,]" which is unique as compared to formal banks where more consideration is given to the "commercial and tax aspects of accounting principles or formal accounting procedures."60 Additionally, hawaladars are able to "exploit naturally

52. Id.
53. Id.
54. JOST & SANDHU, supra note 12 (describing that the primary reason why anyone would bother with hawala is cost effectiveness); see also Wilson, supra note 5, at 3 (describing hawala-type transactions as sometimes benefiting from a better exchange rate and much cheaper than transfers through established, licensed financial institutions); QORCHI ET AL., supra note 3, at 7.
55. JOST & SANDHU, supra note 12; see also Wilson, supra note 5, at 3; QORCHI ET AL., supra note 3, at 7.
56. QORCHI ET AL., supra note 3, at 7.
57. JOST & SANDHU, supra note 12.
58. QORCHI ET AL., supra note 3, at 7.
59. Id. at 8.
60. JOST & SANDHU, supra note 12 (explaining that hawala businesses "operate out of rented storefronts as opposed to bank buildings, which have expensive vault and alarm systems, and may share space with other businesses, further reducing operational expenses").
occurring fluctuations in the demand for different currencies” allowing them to offer their customers rates that are better than those offered by banks. 61

Furthermore, advancements in communication and technology, like fax machines and email, have “greatly benefited” the relative speed in which a hawala transfer can take place. 62 As such, a typical hawala transfer can take, on average, between six to twelve hours and no longer than one or two days, depending on the destination of the payment and the reliability of communication. 63 The speedy hawala system can be contrasted with more sluggish international wire transfer systems or courier services that formal financial institutions employ. 64 Indeed, unlike the informal system used by hawaldars, formal international wire transfer systems that involve banks can take over a week and are hampered by delays due to “holidays, weekends and time differences.” 65

Furthermore, the versatility of hawala transactions makes them an appealing system for remittances in nations where formal banks lack the capacity to provide international or domestic remittance services. 66 Hawala transactions are suited for adapting to “wars, civil unrest, conflicts and economic crisis.” 67 In Afghanistan, for example, where the formal banking

61. See JOST & SANDHU, supra note 12 (describing a hawaldar operating in the United States who is involved in legitimate remittances and could make a profit off an exchange rate margin as small as 2%, making him much more competitive than a bank); see also Looney, supra note 18 (describing that for the “blue collared worker with a monthly stipend of $100, the unofficial hawala system is a far cheaper way to send money back home than the official banking system” where hawala provides a more favorable market exchange rate than the official one).

62. QORCHI ET AL., supra note 3, at 7. “Payment orders can now be sent by facsimile, telephone, or email . . . [and] as the system is based on trust, modern telecommunication is not a requisite. Historically, numerous hawala transactions could be carried out by word of mouth, and reimbursements were based on personal notes, rather than formal documents.” Id.

63. QORCHI ET AL., supra note 3, at 7. These authors note that “transfers between countries where the recipient is in a location with a different time zone or where communications are less reliable require [twenty-four] hours. Slightly more time may be required for payments in more rural regions or villages where the hawaladar does not have a local office or representative.” Id. See also El-QORCHI, supra note 13 (describing that in the hawala system “funds are often delivered door to door within 24 hours by a correspondent who has quick access to villages even in remote areas”); JOST & SANDHU, supra note 12.

64. Id. About a week is required to send “a bank draft from North America to South Asia via a courier service. Surface mail is not an option where the contents are valuable, and can it can also take several weeks to arrive.” Id.

65. Id.

66. QORCHI ET AL., supra note 3, at 9. “The six licensed banks in Afghanistan do not provide any commercial banking services . . . unless they physically move money around the country, most organizations operating in Afghanistan use the informal financial sector to conduct banking business.” Id.

67. Id. at 9. The informal hawala system has existed in conflict-torn regions such as Afghanistan, Iraq, Kosovo and Somalia.
system is not operational, many organizations are forced to resort to IFT systems because commercial banks lack the capacity to service their needs.68 The weakness of local currencies and the rise in the gap between official and parallel markets encourages individuals to rely on IFT systems for funds remittance.69

C. Legitimate vs. Illegitimate Uses

In the preceding discussion, no distinction was made between hawala transactions where the source of the money is legitimate (white hawala) and where the source and intent of the transactions is illegitimate (black hawala).70 Both Interpol and the IMF suggest that such a distinction is important for regulating hawala businesses and enforcing smuggling, money laundering, and terrorist financing legislation.71 While the legitimacy of informal hawala transactions are subject to national legal frameworks, “white hawala” transactions consist mainly of migrant worker remittances, humanitarian relief aid, and personal investments and expenditures.72 “Black hawala” transactions, in contrast, are “almost always associated with a serious offense that is illegal in most jurisdictions” like smuggling, money laundering and terrorist financing.73

1. Migrant Workers Remittances – White Hawala

Global trends suggest that at “around 200 million people migrate annually.”74 International worker migration represents three percent of the global population of six billion.75 Migration flows are likely greater than these

1990’s, which enabled people to transfer funds to Europe or the United States within hours. The Nigeria emigrants are reportedly using the informal system to remit funds to their home country.

Id.
68. Id at 9.
69. Id.
70. JOST & SANDHU, supra note 12. Under Indian and Pakistani terminology, the term “white hawala is used to refer to legitimate transactions.” Id. On the other hand, “black hawala refers to illegitimate transactions, specifically money laundering.” Id.
71. Id.
72. Id. See also QORCHI ET AL., supra note 3, at 12.
73. JOST & SANDHU, supra note 12; see also QORCHI ET AL., supra note 3, at 12. This joint study by the IMF and World Bank chronicled the legitimate versus illegitimate uses of the hawala system. The study indicated that the legitimate uses of the hawala system consist of: (1) humanitarian, emergency, and relief aid in conflict torn countries; and (2) personal investments and expenditures. Illegitimate uses of the hawala system stem from: (1) customs, excise, and income tax evasion; (2) smuggling; (3) money laundering activities; and (4) terrorist financing.
74. OROZCO, supra note 49, at 1. Additionally, migration flows are “not unidirectional . . . Greeks migrate to Germany and the United States, while Albanians migrate to Greece. South Africans move to Australia and England, while Malawians, Mozambiqueans, and Zimbabweans work in South African mines and the service industry.” Id.
75. Id. at 4. “International migration gains greater relevance in light of the significant volume of remittances worldwide.” Id. at 5.
estimates with both skilled and unskilled workers emigrating and global demand for foreign labor increasing. Given the existence of these large migrant-labor communities, the use of the less expensive and more accessible informal *hawala* system is often the only or most convenient option for the remittance of earnings of these migrant laborers to their families. The cheap and swift *hawala* service is in operation "twenty-four hours a day, every day of the year in regions where no banks or financial institutions exist" and, therefore, proves superior to any Western banking operation available to migrant and expert workers.

2. *Humanitarian, Emergency, and Relief Aid – White Hawala*

The *hawala* system is suited for and often is the only option in countries engaged in war or the rebuilding after war. Consequently, the majority of aid organizations operating in these regions turn to the informal financial sector for international or domestic remittance services for humanitarian, emergency, and relief projects. For many humanitarian organizations the "cost and logistical capacity required for the physical transfer of cash is too high" and to fulfill program goals the informal *hawala* system may be the only option.

3. *Personal Investments and Expenditures – White Hawala*

The *hawala* system can often be used to transfer funds for legitimate personal investments and expenditures. For some individuals the *hawala* system is simply the most convenient option for expenditures like “travel,

76. *Id.* at 1.
78. *REZAT*, supra note 44; *see also QORCHI ET AL.*, supra note 3, at 12 (describing *hawala* networks as having “wide coverage, serving far-flung locations, including remote villages in Pakistan and Bangladesh, whereas banks may not handle such a small transaction or reach those remote areas within a reasonable time”).
79. *QORCHI ET AL.*, supra note 3, at 12; *see also SAMUEL MUNZELE MAIMBO*, *THE WORLD BANK, THE MONEY EXCHANGE DEALERS OF KABUL: A STUDY OF THE HAWALA SYSTEM IN AFGHANISTAN* 1 (2003). In Afghanistan, for example, after more than 20 years of conflict, there has been a complete disruption of formal banking and in the absence of any real banking system a large and vibrant informal market has developed. *Id.*
80. *QORCHI ET AL.*, supra note 3, at 12; *see also POLICY AND ADVOCACY UNIT, CARE USA, AFGHANISTAN: OPTIONS FOR HUMANITARIAN ACCESS* 3 (Oct. 2001), http://www.careusa.org/newsroom/specialreports/afghanistan/ahaccess.pdf. “USAID, the single largest donor to the Afghan aid effort, has expressed interest in monetizing some food aid by selling it to Afghan traders.” *Id.* In previous years, “cash has been transferred to communities via the ‘hawala’ system, giving [refugees] the ability to purchase wheat and other necessities through local traders.” *Id.*
81. *QORCHI ET AL.*, supra note 3, at 12. “Humanitarian aid organization staff members carry cash when flying into the country for operational duties, but the amounts involved are usually small and meant for overhead expenses, not program needs.” *Id.*
82. *Id.*
medical care, or college tuition fees. Consider the example of a Dubai-based, Indian-chartered accountant who reported that when he learned his father was being admitted for emergency bypass surgery in India, the "first thing that came to my mind was hawala . . . [T]he money reached my mother before I did." The accountant commented, "who had the time to go to banks and fill out forms? I just went and gave the money and it was delivered to my mom at the door-step within a day."

4. Smuggling – Black Hawala

While the birth of the hawala system may date back centuries, "the growth of the present hawala network has its roots in trading and smuggling operations in South Asia in the 1960's and 1970's." In an effort to "avoid gold import restrictions, traders and smugglers used boats to ship gold from places like the Gulf Cooperation Council (GCC) countries to South Asia." To remit funds back to their countries of origin or purchase more gold, traders and smugglers used the growing population of South Asian nationals working in the GCC countries. For instance, hawaladars in Dubai, in order to settle their liabilities, would finance gold exports to their counterparts and clients in South Asia.

5. Money Laundering Activities – Black Hawala

Hawala and other IFT systems are vulnerable to abuse at each phase of the money laundering process. Interpol has defined money laundering to embody three phases: (1) placement; (2) layering and; (3) integration. The

83. Id.
84. Namita M. Anand, Tainted . . . But on the Move, BUSINESS LINE, Mar. 25, 2002, at http://www.blonnet.com/life/2002/03/25/stories/2002032500070100.htm. "For a maid in Singapore the choice between hawala and the formal banking channels is clear . . . as there are no banks in her village and her parents are not literate, sending money through hawala is simpler, and the hawala operator gives her a better rate." Id.
85. Id.
86. Anderson, supra note 18; see also QORCHI ET AL., supra note 3, at 12 (describing that recent literature attributes the growth of the present hawala network, in part, to gold trading and smuggling operations).
87. QORCHI ET AL., supra note 3, at 12.
88. Id.
89. Id.
90. JOST & SANDHU, supra note 12; see also QORCHI ET AL., supra note 3, at 13.
91. JOST & SANDHU, supra note 12.
methods used to launder the proceeds of criminal and illegal activities become more complex as time progresses and IFT systems, like hawala, are increasingly being used to launder money. The IMF and World Bank have identified several features of IFT systems that can contribute to the placement, layering, and integration of funds. However, both the formal banking sector and the IFT systems are vulnerable to abuse.

The hawala system can provide an effective means of placement of money laundering activities. Hawaladars often operate businesses outside their hawala operations and make periodic bank deposits that can be justified as proceeds from business outside of hawala transactions.

Hawala also serves as an appropriate medium to facilitate layering in the money laundering process as hawala transfers leave a “sparse” and often “confusing paper trail.” From the criminal prospective, laundering money through the formal financial system has the disadvantage of leaving behind documents “that can be traced during an investigation.” IFT systems, like hawala, can minimize detection because the transactions, which are built upon trust, require little or no documentation. Moreover, even when hawaladars maintain records, law enforcement officials cannot readily access them.

In the final phase of money laundering, integration, hawala techniques are also susceptible to abuse. Hawaladars are capable of transforming money into almost any form, making it possible to establish the appearance of legitimacy. The hawala system can be used for money laundering, because the “proceeds can be moved away from the place where a crime was committed

In [the] placement [phase] money derived from criminal activities is introduced into the financial system. . . . In the layering stage, the money launderer manipulates the illicit funds to make them appear as though they were derived from a legitimate source. . . . In the final stage of money laundering, integration, the launderer invests in other assets, uses the funds to enjoy his ill-gotten gains or to continue to invest in additional illegal activities.

Id.

92. QORCHI ET AL., supra note 3, at 13. Current money laundering methods are diverse and can employ both official banking and informal channels, including exchange bureaus, check-cashing services, insurers, brokers, and non-financial traders. Id. See also Ilias Bantekas, The International Law of Terrorist Financing, 97 AM. J. INT’L L. 315 (Apr. 2003) (describing that hawala networks are used primarily by Muslims to send money to relatives, however, authorities believe they also serve as vehicles to launder money, traffic in drugs and arms, and finance terrorists).

93. QORCHI ET AL., supra note 3, at 13. “[N]either system [formal or informal] necessarily involves the physical transfer of funds from one jurisdiction to another. Instead, they depend on a series of accounting debits and credits between the accounts of a network of individuals, companies, accountants, lawyers, and intermediaries.” Id.

94. JOST & SANDHU, supra note 12.

95. Id.

96. Id. See also QORCHI ET AL., supra note 3, at 13.


98. Id.

99. Id.

100. JOST & SANDHU, supra note 12.

to destinations where the transaction can either appear legitimate or from where it can be later brought back to the country through a variety of legitimate routes for the integration process."  

6. Terrorist Financing – Black Hawala

Concerns have been raised about using hawala as an instrument to fund terrorists. The lack of requirements for identification or inquiries into the source is an important facet of hawala transactions. It allows dealers to "facilitate a multiplicity of transfers, which conceal the ultimate origin of the funds through their network in different jurisdictions." For example, international attention was directed at the hawala system when investigators traced an anonymous fund transfer by Al-Qaeda operatives involved in the September 11 terrorist attacks. The fund transfer trail led investigators to a money transfer from a Boston transfer facility to a suspected Al-Qaeda functionary in an exchange house in the United Arab Emirates.

7. Macro-Economic Implications of Informal Fund Transfer Systems

While the direct impact on the policy options of IFT systems is not readily apparent, IMF studies suggest that the impact on a country's domestic "monetary and exchange rate policy choice[s] can be significant." Hawala transactions are not reflected in a country's official statistics as the remittance of funds from one country to another and therefore, are not officially recorded. Consequently, (1) the data available to policymakers does not offer an accurate picture of the "economic and monetary situation of [the] country;" and (2) hawala transactions have fiscal implications for both remitting and receiving countries.

A hawala transaction is intrinsically related to changes in international assets and liabilities in a nation and is, conceptually, part of a country's balance of payment accounts. Therefore, as national authorities are unable to maintain records of informal financial transfers, these informal transactions reduce "the amount of statistical information available to policymakers on the level of economic activity in the country."
Moreover, IFT systems have "fiscal implications" affecting "both remitting and recipient countries." First, as one of the characteristics of hawala indicate, it operates in a largely informal and unregulated environment, thus revenue collection structures for these transactions do not exist. Additionally, as the business settlement accounts between hawala operators are not documented a government "may incur losses in its customs and excise duty revenue."

PART TWO: INTERNATIONAL EFFORTS TO REGULATE HAWALA

A. Introduction

International legislation in the area of IFT systems has concentrated on curbing the tendency for systems like hawala to be used for illegitimate purposes like smuggling, money laundering and terrorist financing. The organization that has emerged as the cornerstone of the international effort to encourage countries to regulate IFT systems like the hawala system is the Financial Action Task Force armed with its legislative initiative titled The Forty Recommendations (The Recommendations).

1. Financial Action Task Force

The Financial Action Task Force (FATF) was created in July 1989 by the governments of the seven major industrial nations (G-7). FATF has been

111. Id.
112. Id. Hawala operations are typically not taxed by the government as they are unrecorded transactions. Id.
113. Id.
116. Jonathan Schaffer ed., The Financial Action Task Force on Money Laundering, ELEC. J. OF U.S. DEPT. OF STATE Vol. 6 No. 2, May 2001, at http://usinfo.state.gov/journals/ites/0501/ijee/fatffacts.htm. The G-7 is currently comprised of the heads of state of Canada, France, Germany, Italy, Japan, the United Kingdom, and the United States. Id. See also WILLIAM C. GILMORE, DIRTY MONEY: THE EVOLUTION OF MONEY LAUNDERING COUNTERMEASURES 79 (1999). At their 1989 Paris Summit, the governments of the seven major industrial nations (G-7) joined by the president of the commission of the European Communities, created FATF to address issues of "drug production, consumption and trafficking" and the "laundering of its proceeds." Id. FATF is now comprised of twenty-nine nations and two jurisdictions, the membership of the FATF includes Argentina, Australia, Austria, Belgium, Brazil, Canada, Denmark, Finland, France, Germany, Greece, Hong Kong, China, Iceland, Ireland, Italy, Japan, Luxemburg, Mexico, The Kingdom of the Netherlands, New Zealand, Norway, Portugal, Singapore, Spain, Sweden, Switzerland, Turkey, The United Kingdom, and the United States, as well as two regional organizations: The European Commission and the Gulf Co-Operation Council. Financial Action Task Force, Members and Observers, at http://www1.oecd.org/
hailed as the "single most important international body in terms of the formulation of anti-money laundering policy." In furtherance of its mission, in 1990, FATF issued a forty-point list of recommendations on money laundering countermeasures. These recommendations constitute an initiative to combat the misuse of financial systems by persons laundering money. They proscribe a range of actions focusing on "improvements in national legal regimes, enhancement of the role of the financial system, and strengthening international cooperation."

FATF places far-reaching responsibilities on financial institutions. The Recommendations encourage the "banking sector to adopt a common position in order to ensure that banks are not used to hide or launder funds acquired through criminal activities." Also, The Recommendations urge financial institutions to make reasonable efforts to: (1) determine the true identity of customers and have procedures for verifying new customers; (2) ensure that business is conducted in conformity with ethical standards, that laws and regulations are adhered to and that a service is not provided where there is good reason to suppose that transactions are associated with laundering activities; (3) co-operate fully with national law enforcement agencies including, where there are reasonable grounds for suspecting money laundering, taking appropriate measures consistent with the law; and (4) implement staff training for procedures for customer identification and for retaining internal records of transactions.

Additionally, in October 2001, FATF expanded its mission beyond money laundering to focus energy and expertise on a worldwide effort to combat terrorist financing. FATF issued Eight Special Recommendations


117. GILMORE, supra note 116, at 79.
118. See Forty Recommendations, supra note 115.
120. See GILMORE, supra note 116, at 86. The common theme concerning recommendations is the view "that financial institutions are the key element in the detection of illicit transactions given their unique function in a country's payments system and in the collection and transfer of financial assets." Id.
121. Id. Recommendations Nine to Twenty-Nine outline a "strategy to engage the financial system in the effort to combat laundering while . . . seeking to ensure the retention of the conditions necessary for its efficient operation." Id. at 86.
122. Forty Recommendations, supra note 115, at 2. See also GILMORE, supra note 116, at 86 (discussing "know your customer" provisions of the FATF Recommendations); Noble & Golumbic, supra note 119, at 119 (stating that Forty Recommendations "advise that financial institutions should refuse to maintain anonymous accounts or accounts with obviously fictitious names").
123. Forty Recommendations, supra note 115, at 5.
124. Id. at 8.
125. Id. at 6.
on international standards for combating terrorist financing and called upon nations to adopt and implement them. Relevant among these recommendations is Special Recommendation VI, dealing with the abuse of alternative remittance systems. This recommendation is based on the presumption that IFT systems, like hawala, have shown themselves to be "vulnerable to misuse for money laundering and terrorist financing purposes." The objective of Special Recommendation VI is to "increase the transparency of payment flows by ensuring that jurisdictions impose consistent anti-money laundering and counter-terrorist financing measures on all forms of money/value transfer systems, particularly those traditionally operating outside the conventional banking sector and not subject to FATF Recommendations." To this end, the special recommendation calls upon:

Each country [to] take measures to ensure that persons or legal entities, including agents, that provide a service for the transmission of money or value, including transmission through an informal money or value transfer system or network, should be licensed or registered and subject to all the FATF Recommendations that apply to banks and non-bank financial institutions. Each country should ensure that persons or legal entities that carry out this service illegally are subject to administrative, civil or criminal sanctions.

Special Recommendation VI consists of three key elements. First, the recommendation calls for jurisdictions to require "licensing or registration of persons (natural or legal) that provide money/value transfer services, including through informal systems." Secondly, the recommendation suggests that

127. Id. The Eight Special Recommendations include:
   (I) Ratification and Implementation of UN Instruments; (II) Criminalizing the Financing of Terrorism and Associated Money Laundering; (III) Freezing and Confiscating Terrorist Assets; (IV) Reporting Suspicious Transactions related to Terrorism; (V) International Co-operation; (VI) Alternative Remittance; (VII) Wire Transfers; (VIII) Non-Profit Organizations.

128. Id.

129. Id. ¶ VI.


131. Id.

132. Special Recommendations, supra note 126, ¶ VI.

133. Interpretive Note, supra note 130. According to the Special Recommendation VI, "licensing means a requirement to obtain permission from a designated competent authority in order to operate a money/value transfer service legally." Id. To this end:
   Jurisdictions should designate an authority to grant licenses and/or carry out registration and ensure that the requirement is observed. There should be an authority responsible for ensuring compliance by money/value transfer services with the FATF Recommendations (including the Eight Special Recommendations). There should also be effective systems in place for
jurisdictions "ensure that money/value transmission services, including informal systems . . . are subject to applicable FATF Forty Recommendations and the Eight Special Recommendations." Finally, the recommendation calls on jurisdictions to impose sanctions on money/value transfer services, including informal systems that operate without a license or registration and "which fail to comply fully with the relevant FATF Forty Recommendations or the Eight Special Recommendations . . ." P

Pursuant to its mission, FATF has taken a unique role by stressing the importance of implementing its initiatives by member and non-member jurisdictions. To this end, FATF has set up four regional review groups to assess the anti-money laundering regulations in a number of jurisdictions against a list of twenty-five "Criteria Identifying Detrimental Rules and Practices that Impede International Cooperation," which FATF compiled in light of the Forty Recommendations and the Eight Special Recommendations.

Following this review, FATF releases a list of non-cooperative countries. After being identified as a "non-cooperative" jurisdiction, FATF urges the "non-cooperative" states to execute measures to improve their legal and financial systems as "expeditiously as possible in order to remedy the . . . deficiencies identified in the reviews." Additionally, in accordance with Recommendation Twenty-One, FATF advises that "[f]inancial institutions should give special attention to business relationships and transactions with persons, including companies and financial institutions," from the non-cooperative countries. Furthermore, FATF announced that should the countries identified as "non-cooperative" fail to make necessary reforms, FATF members may consider adopting countermeasures against such jurisdictions. FATF has also announced its preparedness "to provide technical assistance" to monitoring and ensuring such compliance.

Id. In particular, applicable Recommendations include 10-21 and 26-29. According to the scope and application of Special Recommendation VI, a money or value transfer service may be provided by persons (natural or legal) through the regulated financial system or informally through non-bank financial institutions or through a network or mechanism that operates outside the regulated system, like hawala. See id.


Id. at 3; see also Todd Doyle, Cleaning Up Anti-Money Laundering Strategies: Current FATF Tactics Needlessly Violate International Law, 24 Hous. J. Int'l L. 279, 295 (2002) (describing the four regional review groups to consist of "the Americas, Asia/Pacific, Europe, and Africa and the Middle East").


Id. at 17.

Fifty Recommendations, supra note 115, at 7.

assist jurisdictions in the design and implementation of their anti-money laundering systems.142

Indeed, since the establishment of FATF more than a decade ago, and the subsequent broadening of its mission, FATF has been instrumental in influencing both member and non-member nations in “instituting more rigorous reporting procedures within banks and other financial institutions,” as well as establishing an extensive system of “peer review to assure compliance with FATF guidelines.”143 Generally, FATF strategy has elicited an “immediate response from targeted nations.”144

2. Comments on the Financial Action Task Force Recommendations

However, where FATF is to be commended in its widely adopted approach, the group’s strategy, centered on licensing requirements for hawala and other IFT brokers, does not entirely account for reducing the economic incentives for a country’s citizens and ex-patriots to engage in IFT systems, like the hawala system.145 Registration and licensing requirements, although likely to deter illegal activities, will not succeed in reducing the economic attractiveness of the hawala system.146 The emergence of hawala can be described as a “market response by economic agents to their economic environment.”147 Taken in this context, the international community should apply conclusions reached by the IMF and World Bank and focus its policy goals on combating the economic incentives to engage in hawala transactions. These incentives include: (1) inefficient and inadequate banking infrastructures; (2) lack of comparable alternatives to hawala; and (3) deficient global coordination and capacity building.148

According to IMF and World Bank assessments, the hawala system should be understood as an “informal means of transferring funds” across borders used by individuals “constrained by the level of financial development and government policies” in their home countries.149 Generally, the growth of IFT systems is “negatively correlated with the level of development and liberalization of the formal financial sector.”150 The attraction to IFT systems is increased in countries where inefficient banking institutions operate in environments that include strict foreign exchange controls and heightened state

142. Doyle, supra note 137, at 296.
143. Id. at 294.
144. Id. at 296 (describing that Liechtenstein, the Bahamas, and the Philippines have “each scrambled to review their regulatory schemes and to enact new measures bringing their banking laws up to compliance with FATF standards”).
145. Wilson, supra note 5, at 12.
146. EL-QORCHI, supra note 13.
147. Congressional Hearing, supra note 45, at 44.
148. Id.
149. Id.
150. QORCHI ET AL., supra note 3, at 26.
intervention in the market. Where developed registration and licensing requirements will add a degree of official scrutiny to hawala operators, the ultimate incentives for hawala customers to engage these services will not change. Indeed, "relaxing or abolishing currency restrictions and controls" through "liberalization of interest rates, removal of income taxes on remittances from overseas and lifting restrictions on duties" could encourage business away from hawaladars.

Moreover, current formal remittance systems operating through banks and institutions like Western Union and MoneyGram are not competitive enough to draw customers away from hawaladars. Registration and licensing requirements that are imposed on hawala operators do not address the economic competitive advantage enjoyed by hawaladars, and as long as such discrepancies endure hawala and other IFT systems will "continue to thrive and fill important gaps left by conventional society at the regional and international level[s]." If the formal banking sector intends to compete with the informal remittance business, it should "focus on improving the quality of its service and reducing the fees charged."

Additionally, developing international regulatory standards for IFT systems is a complicated procedure. The growth IFT systems have enjoyed "over many years and across many countries points to the important role that these systems can play in the absence of a robust and efficient formal financial sector." Indeed, "[d]ifferences in the stages of economic" and political development demands that international regulations give consideration to "country specific circumstances and national legal systems." Often, prescribing regulations through licensing requirements will not ensure compliance.

Applying these IMF and World Bank conclusions to efforts to regulate hawala in India, Pakistan and the United Arab Emirates amplifies the weakness

151. Id. See also NIKOS PASSAS, RESEARCH AND DOCUMENTATION CENTRE OF THE DUTCH MINISTRY OF JUSTICE, INFORMAL VALUE TRANSFER SYSTEMS AND CRIMINAL ORGANIZATIONS, A STUDY INTO SO CALLED UNDERGROUND BANKING NETWORKS 70, http://minjust.nl:8080/b_organ/wocd/publications/ivts.pdf (n.d.) (last visited Feb. 15, 2005) (describing that the "faith of Pakistanis in banks and government was undermined when foreign currency deposits were frozen" and "citizens were only allowed to withdraw local currency").

152. Wilson, supra note 5.

153. PASSAS, supra note 151, at 70. But see Wilson, supra note 5 (recognizing that strict foreign exchange controls are important tools of fiscal policy in the hands of governments seeking to stabilize their economy, which also have the effect of encouraging hawala).

154. See EL-QORCHI, supra note 13.

155. PASSAS, supra note 151, at 70.

156. EL-QORCHI, supra note 13. "A longer-term and sustained effort should be aimed at modernizing and liberalizing the formal financial sector, with a view of addressing its inefficiencies and weaknesses." Id.

157. QORCHI ET AL., supra note 3, at 27.

158. Id.

159. Id.

160. Id.
behind a purely economic based strategy. An evaluation of the merits behind these countries strategies will reveal the dual importance economic and political factors can play in a successful strategy to regulate the hawala system.

PART III: HAWALA CASE STUDIES: INDIA, PAKISTAN AND UNITED ARAB EMIRATES

A. India

1. Hawala in India and India’s Response

Estimates indicate that “ten billion of the fourteen billion dollars sent to India each year currently passes through unofficial channels,” like the hawala system. Consequently, the Indian government has adopted firm measures with respect to the regulation of its informal market, in particular the hawala system, with the passage of two acts: The Financial Exchange Regulation Act (FERA) and its later consolidated and amended version, The Financial Exchange Management Act (FEMA). These acts have explicitly prohibited “hawala-type” transactions.

FERA, enacted in 1973, was drafted with the objective of introducing regulations for the entry of foreign capital into India’s economy. It represents the Indian legislature’s efforts to combat the extensive hawala system that continues to flourish in India. As a result of “major changes in the Indian economy and liberalization of industrial and trade policies” in line with India’s changed international economic and trade relations, the Indian legislature saw the “need for a more conducive climate for increased inflow of foreign investment and capital . . . to accelerate . . . growth.” FERA contained certain important “special restrictions in regard to foreign investment and the activities of individuals” engaged in foreign exchange, in particular the hawala system.

Under FERA, sections eight and nine provided “detailed legal prohibitions on the hawala market.” Section eight, for instance, placed

161. Gudka, supra note 18.
162. Foreign Exchange Regulation Act, No. 46 (1973) (India) [hereinafter FERA].
164. Qorchi et al., supra note 3, at 22. “The number of institutions . . . permitted to deal in foreign exchange has been closely defined, and the kinds of transactions permitted for customers . . . have been revised.” Id.
166. Id.
167. Id.
168. Id.
restrictions on individuals who could engage transactions in foreign currency as well as restraints on conversions between Indian currency and foreign currency. In particular, section eight imposed strict licensing requirements on money changers and prohibited the acquiring, borrowing, selling, or transferring of foreign exchange from persons other than an "authorized dealer" in India. Moreover, section eight regulated persons other than authorized dealers or money changers and imposed on them requirements to sell any foreign exchange acquired to an authorized dealer in an effort to legislatively force funds from the informal market into the formal market. Additionally, section nine of FERA specifically covered domestic transactions. Section nine of FERA specifically restricted hawala transactions by prohibiting the making of any payment or credit to any person outside of India without conditional approval from the Indian Reserve Bank. The remaining clauses in section nine of FERA supported the acts "main target of preventing the flight of capital from India through any channel." In 1993, FERA was revised and several amendments were enacted as part of the ongoing process of India's economic liberalization relating to foreign investment and foreign trade for closer interaction with the world economy. Taking into consideration the substantial financial developments in India since the passage of FERA, a bill to replace certain provisions of the act was introduced into the Indian legislature in August 1998. FEMA reintroduces


170. FERA § 8.
171. Id. § 8(1). For purposes of section eight "a person, who deposits foreign exchange with another persons or persons or opens an account in foreign exchange with another person, shall be deemed to lend foreign exchange to such other person." Id.
172. Id. § 8(3). This section provides that:
Where an foreign exchange is acquired by any person, other than an authori[z]ed dealer or money changer, for any particular purpose, or where any person has been permitted conditionally to acquire foreign exchange, the said person shall not use the foreign exchange so acquired otherwise than for that purpose... the said person shall, within a period of thirty days from the date on which he comes to know that such foreign exchange cannot be so used or the conditions cannot be complied with, sell the foreign exchange to an authorized dealer or to a money-changer.
173. Id. § 9.
174. Id. § 9(f). See also FERA § 9(1), explaining that for the purposes of section nine: [W]here any person in, or resident in, India receives any payment by order or on behalf of any person resident outside India through any other person (including an authori[z]ed dealer) without a corresponding inward remittance from any place outside India, then, such person shall be deemed to have received such payment otherwise than through an authori[z]ed dealer.
175. Taxmann's Guide, supra note 169, ch. 5.1; see also FERA § 9.
177. See FEMA.
and expands upon FERA's concept of licenses for moneychangers. In particular, Chapter Two of FEMA prohibits persons from "enter[ing] into any financial transaction in India as consideration for or in association with acquisition or creation . . . of a right to acquire, any asset outside India by any person." Additionally, FEMA provides for a heightened role of the Reserve Bank of India (Reserve Bank) in regulating these transactions by specifying that the Reserve Bank, in consultation with the Central Government, may specify: "(a) any class or classes of capital account transactions which are permissible; and (b) limit which foreign exchange shall be admissible for such transactions."

Additionally, the Reserve Bank, on a limited basis, has attempted to "increase the efficiency and cost effectiveness of banking services" in an effort to make IFT services, like hawala, "seem less attractive." Indeed, bank branch expansions in the 1970s and 1980s improved access to the formal banking sector by reducing the "per branch population." More recently, the Reserve Bank has allowed non-bank financial institutions to undertake "money transfer service schemes to facilitate swift and easy transfer of personal remittances from abroad to beneficiaries in India." These schemes, operating through computerized post offices, are hoped to be more popular because money can now be received in less than ten minutes. Moreover, the Indian Post Office also expects to profit off the service by obtaining ten percent of the share of remittances sent through the facility.

Beyond these measures, the government in India has established a special federal police unit with the sole function to fight economic crime, consistent with FATF Recommendation Twenty-Seven, calling on nations to "ensure that designated law enforcement authorities have responsibility for money laundering and terrorist financing investigations." The unit's mission is to tackle economic crimes like bank fraud and the movement of money from foreign countries through informal fund transfer systems. Furthermore, this

178. See id. at ch. 2; see also Taxmann’s Guide, supra note 169, ch. 5.3.
179. FEMA ch. 2(d); see also QORCHI ET AL., supra note 3, at 22 (describing that the recent FEMA specifically addresses hawala-type transactions by "prohibiting Indian residents from entering ‘into any financial transaction in India as consideration for or in association with acquisition or creation or transfer of a right to acquire any asset outside India by any person’").
180. FEMA ch. 2(a)-(b).
181. QORCHI ET AL., supra note 3, at 23.
182. Id.
183. Id.
184. Id.
185. Id.
186. PASSAS, supra note 151, at 62; see also Forty Recommendations, supra note 115, at 8 (describing institutional and other measures necessary in systems for combating money laundering and terrorist financing).
187. PASSAS, supra note 151, at 62.
unit is designed to target hawala brokers by reducing the amount of money sent through the IFT system as well as diverting funds to the regulated banking industry through strict enforcement of banking laws and extensive investigations of hawala operations.188

2. Assessment of Indian Regulations

Although the Indian government has attempted to tackle its informal fund transfer industry since the early 1970's, its strict legislative guidelines, which essentially ban hawala transactions, have largely backfired.189 This is attributable to several flaws in India's policy and government structure, specifically with respect to the lack of recognition by the Indian legislature that "where strong commercial interests tempt; no amount of legal restrictions will be successful."190 Indeed, the roots of hawala transactions are firmly embedded in the Indian economic and, perhaps more importantly, political atmosphere and has worked to usher in an era of "bad politics" and corruption that has become indicative of the Indian democracy.191

Despite the Indian Government's most restrictive legal provisions, hawala remains a "routine transaction."192 Analysts indicate that people continue to transfer capital outside of India at their "sweet will."193 Indeed, the Indian regulation of hawala is a typical example of where even the most severe licensing provisions cannot ensure compliance.194 Since the Indian rupee continues to depreciate, "wealthy people seeking to protect the value of their wealth have a strong economic interest in transferring their wealth outside India."195

Moreover, the Indian case is unique in that even the most restrictive licensing requirements will have little impact on hawala transactions given the extent of corruption evident in Indian politics.196 Indeed, the Jain Hawala Scandal, which implicated top Indian politicians and bureaucrats for accepting illicit payment through hawala channels, amplifies this point.197 In that case, the Indian Central Bureau of Investigation (CBI), while investigating a case pertaining to funding of Jammu and Kashmir militants, raid[ed] a house in Delhi seizing account books implicating India's rich and powerful, including the Prime Minister at the time, P.V. Narasimha Rao, in receiving funds through

188. Id.
189. See id. (describing that though the liberalization of the Indian economy was supposed to "help fight the prevalence of hawala... the problem continues almost unabated"). Id. at 63.
193. Id.
194. See discussion, supra Part Two B.
196. See KAPOOR, supra note 191, at 84.
197. See id.
India’s illegal hawala market. Twenty-four politicians were ultimately charged with being “beneficiaries of [sixty-four million] rupees in bribes and gifts” from businessmen.

The Indian case, particularly with respect to its hawala scandal, illustrates that a nation’s stage of economic, financial, and political development must be taken into account when formulating regulatory strategies, particularly with respect to IFT systems like the hawala system that are so firmly rooted in that country’s financial and political being. In a developing country like India, criminal elements already exploiting hawala transactions have a strong incentive to infiltrate the political structure to ensure their survival and are able to find willing partners in Indian politicians who “have not seen big money, and they need these funds to win an extremely costly election[s].” Moreover, FATF recommendations, which rely heavily on strong criminal justice infrastructures to enforce licensing requirements, are disadvantaged in India where high ranking Indians are able to escape prosecution unscathed. Indeed, Narasimha Rao survived “numerous corruption scandals in government,” the worst of them being a payment to “escape prosecution in [a] stock market scam.”

B. Pakistan

1. Hawala in Pakistan and Pakistan’s Response

The hawala system in Pakistan operated in a predominantly unregulated environment for years, having only recently come under more focused

198. KAPOOR, supra note 191; see also Jain Hawala Case Rocks India, Mahendra Agaarwal Online, at http://mahendra-agarwalonline.20m.com/PR_JainHawalaCase.htm (Mar. 2, 1996) [hereinafter Jain Hawala Case].

199. Jain Hawala Case, supra note 198. The Jain Hawala case implicated high ranking officials in India including “seven serving Cabinet ministers, all of whom have resigned; the president of the leading opposition Bharatiya Janata Party, who gave up his parliamentary seat; and the chief minister of the local government in New Delhi, who also quit.” Id.

200. See QORCHI ET AL., supra note 3, at 28. In this joint IMF and World Bank study the authors conclude that for the regulation of the hawala system will among other things depend on “the ability of the formal financial sector to respond to the legitimate market demand for hawala type transactions.” Id. This conclusion can be expanded, using the Indian case, to include comprehensive political reforms to ensure compliance with regulations.

201. KAPOOR, supra note 191, at 88.

202. See id.

203. Hard Times, NEWS INSIGHT, Oct. 8, 2003, at http://www.indiareacts.com/archivedebates/nat2.asp?recno=736&ctg=. “Although there is no rule on the effect of corruption charges on political careers in India few politicians are said to hit rock bottom.” Id.

204. See Experts Urge Measured Regulation of ‘Hawala’ Monetary Transfers, ARAB AMERICAN BUSINESS, at http://www.arabamericanbusiness.com/June2002/intbus_expertsurgemeasured.htm (n.d.) (last visited Sept. 27, 2003) [hereinafter Arab American Business]. “Mohammed al-Qorschi, a senior economist with the International Monetary Fund,” reported that Pakistan alone “received around $5 billion a year through paperless transactions.” Id.
Indeed, it has been reported that the State Bank of Pakistan (SBP), prior to undergoing policy refinements, had periodically made large “outright dollar purchases from offshore moneychangers.” Moreover, with a large number of Pakistanis living abroad and seeking to remit funds back to Pakistan, the Pakistani economy has undergone “a long history of various forms of capital controls.” To this end, Pakistan has “tried to encourage capital to stay in Pakistan” or eventually flow into the regulated financial system through two early initiatives: (1) the Foreign Exchange Bearer Certificates (FEBCs) Scheme in 1985; and (2) the Foreign Currency Bearer Certificates in 1992 (FCBCs). The aim of these initiatives was to “attract funds from Pakistanis abroad and to reduce the attraction of hundi and the hawala networks in the country.”

Post September 11, Pakistan, under pressure from the United States and the International Community, has “crack[ed] down on money laundering and regulating the hawala fund-transfer system.” The SBP recently issued a report titled, “Islamic Finance and Pakistan’s Efforts in the Financial War on Terrorism,” which highlighted Pakistan’s revitalized effort in the financial war on terrorism and money laundering. In that report, Pakistan details its revised approach to banking through adopting the recommendations of FATF and “actively participating as a member” of that group’s regional Asia-Pacific Group on Money Laundering. Indeed, Pakistan, after reviewing its existing banking systems and procedures, has developed a “multiple track strategy” to reign in hawala markets, the main elements of which include: (1) the development of comprehensive legislation to fill in the gaps and loopholes in the existing laws, and “empower and streamline the procedures for monitoring, detection, reporting, investigation, [and] prosecution of offenses;” and (2) the


207. QORCHI ET AL., supra note 3, at 22.

208. PASSAS, supra note 151, at 63-64. The FCBCs were “timed rather badly” as its “issuance coincided with the close down of . . . a bank managed by Pakistani’s . . . amid accusations of unprecedented fraud, corruption and money laundering.” Id.

209. Id.


212. Id.
strengthen the regulatory and supervisory capacity of the Pakistani government.  

Under the first element of Pakistan’s strategy the informal market will be allowed to “co-exist along with the conventional banks.” To this end, the Governor of the SBP has prepared a draft act that conforms to FATF standards. The law would require profiling of all the account holders, “both existing and new, to detect suspicious transactions.” These measures are an in conformity with FATF Recommendations Thirteen and Fourteen calling on nations to encourage reporting of suspicious transactions. Moreover, Pakistan’s new profiling procedures are consistent with FATF Recommendations designed to curb the anonymity associated with hawala transactions by calling on financial institutions to “undertake customer due diligence measures, including identifying and verifying the identity of . . . customers.”

Within Pakistan’s strategy to develop comprehensive legislation, Pakistani President Pervez Musharraf’s government passed a law that requires “hawala dealers to register with the government and document their transactions.” This law is consistent with FATF Special Recommendation VI containing a core requirement for jurisdictions to require licensing or registration of persons that provide money transfer services. The newly promulgated legal framework calls for the “transformation of money changers into foreign exchange companies” and “allows money changers a two-year period to register” and comply with the new rules.

Under the second element of Pakistan’s comprehensive strategy, the SBP, Securities Exchange Commission of Pakistan (SECP), and the National

---

213. Id.
214. Id. ¶ 2
215. Malik, supra note 206.
216. Id.
217. Forty Recommendations, supra note 115, at 5. FATF Recommendation Thirteen states that:
If a financial institution suspects or has reasonable grounds to suspect that funds are the proceeds of a criminal activity, or are related to terrorist financing, it should be required, directly by law or regulation, to report promptly its suspicions to the financial intelligence unit.

Id.
218. Forty Recommendations, supra note 115, at 2. This recommendation calls on financial institutions to “not keep anonymous accounts or accounts in obviously fictitious names.” Id.
220. Id. See also Interpretive Note, supra note 130 (describing that Special Recommendation VI consists of three core elements).
221. QORCHI ET AL., supra note 3, at 22.
Accountability Bureau (NAB)\textsuperscript{223} have developed distinct and identifiable responsibilities consistent with FATF recommendation Twenty-Seven.\textsuperscript{224}

Under the new system, the State Bank of Pakistan will be responsible for regulation, supervision, detection and reporting in respect of all the banking institutions; SECP for non-bank finance companies and NAB for investigation and prosecution. [The] Anti-Narcotic Force already has the authority and powers to investigate and prosecute drug-related money transactions.\textsuperscript{225}

Moreover, Pakistan's banking reforms have come at the heels of a political overhaul of the Pakistani government led by General Parvez Musharraf.\textsuperscript{226} Musharraf, who orchestrated a bloodless coup in October 1999 against the then Prime Minister Nawaz Sharief,\textsuperscript{227} introduced a series of sweeping amendments to the Pakistani Constitution which his government anticipates will lay the groundwork for a "fair and clean[] democracy [in Pakistan] and . . . block corrupt and incapable politicians from participation in . . . election[s]."\textsuperscript{228} Whether Musharraf has delivered on his promise of a "fair and clean" democracy in Pakistan is far from decided. However, the impact of Musharraf's government's on the Pakistani economy, which is projected to grow this year at a rate of 4.5 percent is undisputed.\textsuperscript{229} Indeed, "fiscal austerity" and political reform measures imposed by Musharraf's government have led to increased tax revenues, low interest rates and a shrinking national debt in Pakistan.\textsuperscript{230} Another positive feature with respect to

\begin{itemize}
\item \textsuperscript{223} See National Accountability Bureau of Pakistan, \textit{at} http://www.nab.gov.pk/ (last modified Mar. 7, 2005) (last visited Mar. 24 2005). The NAB was established in Pakistan in 1999 pursuant to a Presidential Ordinance calling for a "free, transparent, and across the board accountability" of cases involving "corruption, corrupt practices, misuse/abuse of power, misappropriation of property and kickbacks." \textit{Id.}
\item \textsuperscript{224} See \textit{HUSAIN}, supra note 211, \textsection 2; see also Forty Recommendations, \textit{supra} note 115, at 8. That recommendation stresses that "countries should ensure that designated law enforcement authorities have responsibility for money laundering and terrorist financing investigations." \textit{Id.}
\item \textsuperscript{225} \textit{HUSAIN}, \textit{supra} note 211, \textsection 2.
\item \textsuperscript{227} To many outside observers the coup against Prime Minister Nawaz Sharief was no surprise as Shareif was widely recognized as incapable of "significantly reducing corruption, improving living standards, or constructively managing political dissent in Pakistan." \textit{Id.}
\item \textsuperscript{230} \textit{Id.}
\end{itemize}
Pakistan’s economy is Pakistani rupee’s health which “has gained 11% against the greenback since September 11, largely because of a crackdown on the black market hawala system of money transfers, as part of the war on terror.” As a result, the country’s foreign exchange reserves have topped $9.5 billion for the first time, giving the Pakistani rupee unusual strength.

2. Assessment of Pakistani Legislation

Contrary to the Indian example, the initial assessment of the Pakistani Government’s efforts to regulate hawala transactions appears positive. After the implementation of reporting requirements and simultaneous initiatives by the SBP, “thousands of dealers across Pakistan have watched their thriving businesses falter and in some cases collapse.” Moreover, since the change in policy official remittances have tripled. Indeed, the SBP has seized the opportunity to increase official remittances and has instituted systems to maintain a database of all remittances and “introduce[ed] a handful of new products” that will ensure delivery of cash quicker.

The reason for Pakistan’s success can be attributed to its successful recognition of the policy goals necessary to regulate hawala transactions beyond mere licensing of hawaladars. Indeed, coupled with Pakistan’s licensing requirements were initiatives to improve the SBP banking practices, particularly, allowing the informal market to co-exist with formal banks for a period of time as well as the implementation of successful fiscal austerity measures to improve Pakistan’s economic standing. With obvious disincentives for the use of the hawala system, expatriate Pakistanis have been


232. Id. See also Imtiaz Gul, Boom Time for Pakistani Economy, ECONOMY NEWS, Sept. 2, 2003, at http://english.aljazeera.net/NR/exeres/F5C15088-CB1D-4278-97F7-7C60F33132F5.htm. In 2001, the rupee fell 23% against the U.S. dollar and in the 1990s, foreign investors lost an average of 8% to 10% on their investments every year on account of the depreciation of the rupee; “this year, for the first time, they won’t — and this is a very good trigger from them to look at Pakistan.” Id.


234. Id. Forex Association of Pakistan, a Karachi-based trade group, reports that hawala business has been reduced by 75% in Pakistan. Id.

235. Id. “According to the most recent figures available from the State Bank of Pakistan, monthly remittances [through the formal sector] climbed to 260 million, from an average of 80 million.” Id. The treasurer of Habib Bank, “Pakistan’s second-largest bank, estimates that official remittances will rise from $1.07 billion last year to $2 billion by the end of fiscal 2002. Within the next two to three years . . . they could hit $5 billion.” Id.

236. Id. “Habib-Bank has automated its systems to maintain a database of all remittances and is introducing a handful of new products that will ensure delivery of cash within 24 hours.” Id.

237. See supra discussion Part Two B.

238. Id.
routing their remittances through the banking system instead.\textsuperscript{239}

However, a more evident difference between the Indian and Pakistani strategy rests in the differing political situations in each country. In Pakistan, "history has shown that military [g]enerals . . . are more skillful and diplomatic" than politicians.\textsuperscript{240} Musharraf's government has been able to swiftly and effectively install fiscal precision and political reform measures that have helped reduce the economic incentives for both expatriate and resident Pakistani's to engage in \textit{hawala} in Pakistan.\textsuperscript{241} Indeed, contrary to the case in India, where decades of corruption have bred more corruption, destabilizing efforts to reign in \textit{hawala} transactions, Pakistani leaders have taken advantage of the political climate in Pakistan to implement balanced legislation. This has had a marked deterrent effect on Pakistan's economic incentives to engage the \textit{hawala} system.

C. United Arab Emirates (UAE)

1. \textit{Hawala} in UAE and UAE Response

The UAE has been described as the third leg in a \textit{hawala} triangle encompassing India and Pakistan.\textsuperscript{242} Dubai is regarded as a "key point in the global \textit{hawala} network" due, in part, to the "large presence of expatriate workers and businessmen there."\textsuperscript{243} Post-September 11, Western nations, led by the United States, have alleged that chief terror suspects of the Al-Qaeda network "transferred funds through the \textit{hawala} [system] . . . and the United Arab Emirates (UAE) was cited as a transit point from where most of the money spent by the individuals behind the Sept[ember] 11 terror attacks was reportedly transferred."\textsuperscript{244} As a consequence, the UAE was placed on FATF's "watch list" in the months following September 11.\textsuperscript{245}

Partly in response to international pressure, the UAE Central Bank,\textsuperscript{246} in

\begin{itemize}
\item 239. See Pakistan Cripples, supra note 233.
\item 240. UI Hassan, supra note 228.
\item 241. See id.
\item 242. See Pakistan Cripples, supra note 233. \textit{Hawala} "is an extensive international money transfer system based around the triangle of Pakistan, Dubai and parts of India." \textit{Id.}
\item 243. Raveenran, supra note 105, at 5. In the United Arab Emirates (UAE) \textit{hawala} "often takes the form of flight of capital resulting from exchange controls, regulations against outflow of funds and other policies followed by many Asian countries, including India." \textit{Id.}
\item 245. Raveenran, supra note 105.
\item 246. See The Monetary System and Organization of Banking, No. 10, art. 5 (1980) (U.A.E.). The function of the UAE central bank is laid out in this statute:
\end{itemize}

\textquote{The Bank shall direct the monetary, credit and banking policy and supervise over its implementation in accordance with the State's general policy and in such ways as to help support the national economy and the stability of the currency. For the attainment of its objectives, the Bank shall: (1) exercise the privilege of currency
May 2002, hosted the first international conference on *hawala*. Over three-hundred delegates representing regulatory bodies, law enforcement agencies, supranational institutions, banks, and money changers from nearly forty participating countries gathered in Abu Dhabi to map an effective regulatory strategy for *hawala*. The conference, hosted by the UAE Central Bank National Anti-Money Laundering Committee, culminated in the “Abu Dhabi Declaration” recognizing the need for a regulatory and supervisory system through licensing for *hawala* transactions while simultaneously acknowledging that *hawala*, as a system, “has some positive aspects” that should not be banned. Following the recommendations of the conference, the UAE Central Bank revised its resolutions regarding the regulation of financial and monetary...
intermediaries. To this end, the "Central Bank had recently issued 61 certificates to hawala brokers while another 22 brokers will be registered in the coming period."

The UAE has had formal banking regulations and supervision for non-bank remitters' operators since the 1980s with passage of Union Law No. 10. Subsequent resolutions to the laws permit moneychangers to be licensed as "money remitters." Under the law, "hawala operators must record details of persons or institutions that transfer an amount . . . of 2,000 [Dirhams] or [its] equivalent in other currencies." Additionally, the law requires particular documentation to be used by hawaladars for customer identification purposes. In transfers of less than 2,000 Dirhams, the transferor should be issued a receipt.

Moreover, in January 2002 the UAE passed an anti-money laundering law imposing restrictions on monetary transfers. The council of Ministers of the UAE approved the UAE Anti-Money Laundering Law, which makes the laundering of property derived from unlawful means a criminal offense. Relevant provisions of this act call for: (1) the creation of a "financial information unit" to deal with money laundering and suspicious cases;

---

251. See United Arab Emirates Cent. Bank Bd. ofDirs., Cent. Bank of the United Arab Emirates, Regarding the Regulation for Financial and Monetary Intermediaries—Resolution No. 126/6/95 (1995); United Arab Emirates Cent. Bank Bd. ofDirs., Cent. Bank of the United Arab Emirates, Regarding the Regulation for Financial and Monetary Intermediaries—Resolution No. 153/5/97 (1995). 252. U.A.E. Defends Hawala System, UAE Interact—The Official Website for the Ministry of Information and Culture of the UAE, at http://www.uaeinteract.com/news/default.asp?cntDisplay=10&ID=220 (last visited Apr. 10.2005). 253. See The Monetary System and Organization of Banking, No. 10 (1980) (U.A.E.); see also Qorchi et al., supra note 3, at 25. 254. United Arab Emirates Cent. Bank Bd. ofDirs., Cent. Bank of the United Arab Emirates, Regarding Regulating of Money Changing Business in the U.A.E—Resolution No. 123/7/92, art. 2 (1992) [hereinafter Resolution 123/7/92]. This resolution provides for a licensing requirement in the United Arab Emirates stating that "no person, whether natural or juridical, shall carry on money changing business in the United Arab Emirates unless he is licensed in writing by the Governor of the Central Bank to do so in accordance with this Resolution or unless he is exempted from the provisions thereof." Id. See also Qorchi et al., supra note 3, at 25. 255. Qorchi et al., supra note 3, at 25; see also Resolution 123/7/92, supra note 254, art. 4(2); Press Release, Central Bank of the United Arab Emirates, Anti-Money Laundering New Law, at http://www.cbuae.gov.ae/Releases/AntiMoneyLaundering2.htm (n.d.) (last visited Oct. 29, 2003). The central bank through a decision of its Board of Directors reduced the thresholds for official identification to 2,000 Dirhams from 200,000 Dirhams for moneychangers. Id. 256. Qorchi et al., supra note 3, at 25. The law requires that the documents listed be used for customer identification: "(1) passport; (2) U.A.E. ID card for U.A.E nationals; (3) labor card for non-U.A.E. nationals; or (4) driver’s license." Id. 257. Id. 258. Id. 259. UAE Anti-Money Laundering Law, at art. 7. This article states that: [T]here shall be established, within the Central Bank, a unit named the ‘financial information unit’ to deal with money laundering and suspicious cases, and to
(2) agencies “concerned with licensing and supervision of financial institutions or other financial, commercial and economic establishments” to establish “mechanisms to ensure compliance of those institutions.”

2. Assessment of UAE Legislation

The UAE has largely followed Pakistan’s strategy of balanced regulation of hawala through licensing while also making additional efforts to address weaknesses that may exist in the formal sector. Like Pakistan, the UAE recognized that “[o]ver-regulation or, indeed, making [hawala] illegal would not work . . . [i]t would drive the business[es] underground” like the case in India. However, as the UAE, distinct from India and Pakistan, is primarily a hawala remitting country, its regulatory approach must have an increased focus on effective law enforcement and improved service quality in order to deter hawala transactions at their source.

Unlike the Indian and Pakistani cases, the UAE enjoys a heightened quality of political stability and formal financial sector security, each of which, as has been demonstrated in India and Pakistan, has an important influence on the regulatory attitude toward hawala. As the UAE is primarily a hawala-remitting country, the regulatory scheme adopted by UAE authorities recognizes this fact, and its supervisory interest stems primarily from concerns

which reports of suspicious transaction shall be sent from all financial institutions and other financial, commercial and economic establishments. The committee shall determine the format for reporting suspicious transactions and methods of communicating reports to the said unit. The said unit shall render the information available with it at the disposal of law enforcement agencies to facilitate their investigations. The said unit may exchange information on suspicious transactions with their counterparts in other countries in accordance with international conventions to which the state is party, or on the basis of reciprocity.

Id.

260. U.A.E. Anti-Money Laundering Law, art. 11. This article states that: [A]gencies concerned with licensing and supervision of financial institutions or other financial, commercial and economic establishments are required to establish appropriate mechanisms to ensure compliance of those institutions with anti-money laundering rules and regulations in the state. This should include reporting of suspicious cases, upon detection thereof, to the unit stated in Article 6 herein.

Id.

261. See Interview by International Herald Tribune with Sultan bin Nasser Al-Suwaidi, the United Arab Emirates Central Bank Governor (Oct.10, 2003).

262. Id. Sultan bin Nasser Al-Suwaidi, the UAE Central Bank Governor, recognized the challenge he faced was to: [C]reate a system that enabled the many people, particularly foreign workers, who have used the [h]awala system for legitimate purposes, to continue doing so, while making it as difficult as possible for those who want to abuse the [h]awala system for illegal purposes.

Id.

263. See QORCHI ET AL., supra note 3, at 25.

264. Id. at 27.
about hawala’s potential for abuse. Consequently, the UAE has cooperated with international efforts to prosecute criminal hawala operations, in particular with respect to the international effort against Al-Barakaat, a Somali-based hawala operation. Al-Barakaat had locations in over forty countries and used its hawala system to provide “material, financial and logistical support” to terrorist groups through its financial center located in Dubai. The UAE, coordinating with the United States Department of Treasury, was able to successfully block Al-Barakaat’s assets in Dubai, disrupting the organizations cash flow in excess of sixty-five million dollars. Indeed, the UAE’s balanced legislative and enforcement technique worked to successfully undermine the financial power of trafficking networks and organized crime, amplified by the case of Al-Barakaat.

CONCLUSION

Hawala transfers provide a cost effective, speedy, reliable, and trustworthy method for remittances. The hawala system has survived because of its demonstrated resilience in a banking market that is both competitive and efficient. The mechanics behind a typical hawala transfer, consisting of transactions across international lines involving multiple currencies and settlement procedures, do not differ from other remittance systems, the only derogation being hawala’s existence in the informal realm. Having legitimate purposes, such as worker remittances, humanitarian relief and personal investment expenditures, hawala plays an important role in many nations. However, like any other financial system, hawala’s susceptibility to abuse for illegitimate purposes, like smuggling, money laundering, and terrorist financing has drawn serious criticism from the international community.

The Financial Action Task Force, a creation of the Group of Seven Industrialized Nations, has taken the lead in modeling and recommending that countries adopt legislation to regulate informal fund transfers, including hawala. FATF’s list of Forty Recommendations and subsequent addition of Eight Special Recommendations has served as the benchmark for domestic efforts to regulate the informal banking sector. FATF’s active role in identifying, reviewing, and sanctioning non-compliant countries has served as motivation for nations to adopt FATF style policies based on licensing of individuals engaged in the informal business transactions. However, FATF recommendations fail to account for several economic incentives inherent in the hawala system. A detailed study of India, Pakistan, and the UAE reveals the

265. Id. at 27.
267. Id.
268. Id.
269. Id.
importance of a country's economic and political environment in reigning in the hawala system.

India's strict approach to regulating its informal economy, amounting to an all-out ban on hawala, had poor results. Due, in part, to India's corrupt democratic system, India's legislative efforts to curb hawala transactions have largely been underscored, despite its attempts to implement many FATF recommendations. This result can be explained by deficiencies in FATF's recommendations that fail to account for political reforms necessary in many hawala remitting and receiving countries. Conversely, more recent efforts by Pakistan and the UAE have seemingly accounted for the Indian mistake of over regulation and have attempted to reign in hawala transactions through gradual licensing requirements coupled with financial and political sector reforms, offering competitive remittance alternatives to hawala. In Pakistan, for instance, efforts to regulate hawala took shape after a political overhaul of the Pakistani government. Additionally, successful cooperative efforts to reign in criminal hawala enterprises based in the UAE highlight the important role hawala remitting countries play in the hawala regulatory effort.

Given these considerations, countries seeking to regulate their hawala markets would serve themselves well by examining India, Pakistan and the UAE as examples of both effective and ineffective polices and legislation. Pakistan and the UAE have recognized the inherent economic incentives to engage in hawala and have taken advantage of their domestic political climates to implement balanced legislative and political reforms that recognize and respond to these incentives. Other net hawala remitting and receiving countries should follow suit and implement similar balanced economic and political responses.