

SNR & COMPANY
CHARTERED
ACCOUNTANTS

A background image showing a person's hand holding a gold pen over a calculator. The image is overlaid with various data visualization elements, including a line graph with a peak, a bar chart, and a grid pattern. The overall color scheme is teal and white.

LEGAL UPDATE

15th May 2023

BACKGROUND

The Prevention of Money Laundering Act, 2002 (PMLA) forms the core of the Indian legal framework put in place to combat money laundering. PMLA and the Rules notified there under came into force with effect from July 1, 2005. Director, FIU-IND and Director (Enforcement) have been conferred with exclusive and concurrent powers under relevant sections of the Act to implement the provisions of the Act.

The PMLA impose obligation upon the reporting entities, to verify the identity of clients, maintain records and furnish information to FIU-IND and ED. The term 'reporting entity' has been defined in Section 2(1)(wa) of the PMLA to include banking companies, financial institutions, and intermediaries and *'persons carrying on a designated business or profession'*.

Further, section 2(1)(sa) of the PMLA defines the term *'person carrying on designated business or profession'*. As per this clause, various class of persons such as Inspector-General of Registration, real estate agent, dealer in precious metals have been included. Further, clause (vi) of Section 2(1)(sa), empowers the Central Government to designate any other person carrying on certain activities to mean *'person carrying on designated business or profession'* by issuing a notification to that effect.

Notification dated 3rd May 2023

With the intention of strengthening the PMLA, the central government has exercised the powers given by section 2(1)(sa) and issued a notification dated 03rd May 2023 stating that the financial transactions in relation to the following activities carried out by practicing chartered accountants ('CAs'), company secretaries ('CSs') and cost & works accountants ('CWAs') on behalf of their clients, shall be activities for the purposes of Section 2(1)(sa):

- Buying and selling of any immovable property.
- Managing client money, securities, or other assets.
- Management of bank, savings, or securities accounts.
- Organization of contributions for the creation, operation, or management of companies.
- Creation, operation, or management of companies, limited liability partnerships, or trusts, and buying and selling of business entities.

Further, while defining the 'relevant person', the government has specifically included the firms constituted by these professionals.

Notification dated 9th May 2023

In furtherance of the earlier notification dated 3rd May 2023, the Central Government has issued another notification dated 09th May 2023 wherein the scope of activities carried out in the course of business or on behalf of or for another person has been clearly specified. Thus, the provisions of PMLA shall be attracted upon a reporting entity carrying out the following activities:

- Acting as a formation agent of Companies and LLPs;
- Acting as (or arranging for another person to act as) a director or secretary of a company, a partner of a firm or a similar position in relation to other companies and limited liability partnerships;
- Providing a registered office, business address or accommodation, correspondence or administrative address for a company or a limited liability partnership or a trust;
- Acting as (or arranging for another person to act as) a trustee of an express trust or performing the equivalent function for another type of trust; and
- Acting as (or arranging for another person to act as) a nominee shareholder for another person.

Having said this, the notification dated 09th May 2023 has also listed certain activities that shall not be regarded as activities for the purpose of section 2(1)(sa). They are as follows:

- Any activity that is carried out as part of any agreement of lease, sub-lease, tenancy or any other agreement or arrangement for the use of land or building or any space and the consideration is subjected to deduction of income-tax as defined under section 194-I of Income-tax Act; or
- Any activity that is carried out by an employee on behalf of his employer in the course of or in relation to his employment; or
- Any activity that is carried out by an advocate, a chartered accountant, cost accountant or company secretary in practice, who is engaged in the formation of a company to the extent of filing a declaration as required under section 7(1)(b) of the Companies Act, 2013; or
- Any activity of a person which falls within the meaning of an intermediary as defined in section 2(1)(n) of the Prevention of Money-laundering Act, 2002 (15 of 2003).

Rationale for changes

It seems that these changes have been made in response to various Chinese companies being formed with Indian directors/ shareholders defeating the restriction imposed by the Indian Government of getting prior approval. Some accounting and secretarial professionals assisted in setting up these companies. These professionals used their office addresses to register these shell companies and even became directors, with some having operational authority to operate their bank accounts.

To prevent such scams, CA, CS, and CWA are now required to perform due diligence on their clients' ownership, financial status, and source of funds, as well as document the transaction's purpose.

The change in PMLA law also assumes significance ahead of the proposed assessment of India under the Financial Action Task Force (FATF) expected to be undertaken later this year. The FATF is the global money laundering and terrorist financing watchdog. India's possible onsite assessment is slated for November, while the assessment is likely to come up for discussion in the plenary discussion in June next year.

Repercussions

As per Chapter IV of the PMLA read with the Prevention of Money-laundering (Maintenance of Records) Rules, 2005, now these professionals are required to comply with the following obligations:

- Verification of their client's identity as well as their beneficial owners.
- Maintain records of all transactions in the prescribed manner for a period of 5 years from the date of the transaction
- Maintain record of documents evidencing their client's identity as well as the identity of their beneficial owners and also keep account files and business correspondence relating to the clients, for up to 5 years after the termination of business relationship with the client.
- Carry out enhanced due diligence for certain specified transactions as per Section 12AA.
- Provide access to the records maintained to the Enforcement Directorate ('ED').



Our Offices:

SNR & COMPANY
CHARTERED
ACCOUNTANTS

Delhi (Head Office)

A-15, Second Floor Hauz Khas, New
Delhi - 110016

Phone: +91-11- 41655801, 41655802

Pune

Office no 2A, Gangotri Complex,
927, Synagogue Street, Camp,
Pune - 411001

Phone: +91 020 30492191

Bangalore

No - 5A, Second Floor, 6th Main, KHB Colony,
Basaveshwaranagar Bangalore Karnataka -
560079

Phone: +91 80 42064178

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