UPES

UNIVERSITY OF PETROLEUM & ENERGY STUDIES

Centre: Dehradun

Examination	: **End Semester Examination May 2019**	Semester: **II Semester**
Programme & Branch	: **MBA IB**	Duration: **3 Hours**
Course Code	: **INTB 7003**	Max. Marks: **100**
Course Title	: **Foreign Exchange Management & Trade Finance**	

Section A

Answer all the questions — **10 X 3 = 30 Marks**

1. Today you contract to buy US $ 30 days forward at 66.98 Rs/1$. Suppose 30 days from now when the forward contract matures, the prevailing spot exchange rate is 68.5 Rs/1$. Have you gained or lost by holding the forward contract? Suppose instead the prevailing spot rate is 66.01 Rs/1$. Have you gained or lost by holding the forward contract? **(CO2)**
2. US$ /INR = 66.98/00; US$/CHF = 1.01 /15 Hence, CHF/INR = ? **(CO1)**
3. What are the two plans were taken up at the Bretton Woods Conference in July 1944 and explain briefly. **(CO3)**
4. Compare SDR with Bancor? **(CO1)**
5. Why did countries start to float their currencies during non-system? **(CO1)**
6. Brief the purchase and repurchase of IMF lending. **(CO2)**
7. What is law of one price? **(CO1, 2)**
8. What is ‘J’ curve effect of Marshall-Lerner? **(CO1, 2)**
9. Compare FEMA with FERA. **(CO3)**
10. What are the functions of Enforcement Directorate? **(CO3)**

Section B

Answer any three questions — **3 X 15 = 45 Marks**

1. What is Big Mac index? The price of a Big Mac in the U.S.A. was $3.57. The price of a Big Mac in the Euro Zone was € 3.31. What is the implied PPP? The actual exchange rate was $1 = € 0.94. Is Euro overvalued of devalued? If so, how much in percentage? Why do we measure Big Mac index? **(CO2)**
2. Compare the covered interest rate parity with uncovered interest rate parity? **(CO1)**
3. What are objectives of FEMA? How the foreign exchange moves out of the country and moves in to the country through trade based money laundering practices? **(CO4)**
4. Why the integration of cash and trade is needed? How do you evaluate the different techniques of funding for trade transactions and wider working capital? **(CO4)**

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Section C

Answer all the questions **1 X 25= 25 Marks**

Money laundering through banks

By B V Kumar, Former Member, CBEC

Human ingenuity, creative imagination and expertise have produced infinite varieties of laundering schemes. They are as varied as, the modus operandi adopted in smuggling contraband. Banks and Financial Institutions which have access to international money transfers are a vital link and facilitate international trade in goods and services. They are used by the governments, multi-national corporations, tourists and ordinary citizens. Banks and financial institutions, being generally open to public transactions, are also accessible to organized crime, drug traffickers, terrorists and white collar criminals.

Normally, the banking sector does not attract attention of the law enforcement agencies for unlawful activities, unless there is specific intelligence about the persons utilizing the banking system either for criminal activity, fraud, for transfer of funds generated in crime or the involvement of the banking personnel in such activities. In 1995, one of the biggest money laundering operations using the banking system was detected by the Directorate of Revenue Intelligence (DRI). Subsequently, follow up investigations conducted by the Foreign Exchange Enforcement Directorate (ED) revealed extensive involvement of a number of banks and individuals abusing the facilities available through the banking system.

Intelligence received by the DRI indicated that the South Indian Bank Ltd., Nariman Point Branch, Bombay was involved in a massive money laundering operation. Enquiries conducted revealed that a number of fictitious accounts were opened in the bank for depositing large amounts of currency which in turn were being remitted to Hong Kong, against fraudulent documents, ostensibly, covering legitimate imports. One of the accounts was in the name of M/s Chinubhai Patel & Co. said to be existing at 27, Vaishali Shopping Center, JVPD, Bombay - 49, with the South Indian Bank Ltd., Nariman Point Branch, Bombay. Enquiries conducted revealed that the account was opened in February 1994 and the party was introduced by the Bank Manager Mr. Kasturi Rangan. The Bank Manager did not follow the instructions of the Reserve Bank of India (RBI), and the account was opened without obtaining the photograph of the account holder.

Verification of the address revealed that the firm M/s Chinubhai Patel & Co., did not exist at that address. This account was utilized for depositing cash of Rs. 387,379,000/- and from his account remittance equal to US $ 12,048,650/- was remitted to Hong Kong in favour of M/s R.P. Imports and Exports, Hong Kong. The remittances were made on the basis of fraudulent documents. Further investigations conducted by the DRI in India and abroad, revealed that four more firms have been operating their accounts in a similar manner in the South Indian Bank Ltd., and these firms were identified as M/s Rakesh International, M/s R.M. International, M/s P.M. International and M/s Deepee International. These firms were also found to be fictitious and not existing at the given address. They were operating the account with the said bank from June 1992, onwards. Through this account an amount equivalent to US $ 80 million, approximately equivalent to Rs 2500 million, was transferred from India to Hong Kong. The identity of the Hong Kong firm is under investigation.

Investigations conducted so far by the Directorate of Revenue Intelligence have revealed that certain persons, including Rajesh Mehta and Prakash, had opened bank accounts solely for the purpose of depositing cash and then transferring the said funds in foreign exchange to countries like Hong Kong, Singapore and Dubai, in a fraudulent manner through the South Indian Bank Ltd., Nariman Point Branch, Bombay and for this purpose they were using fictitious addresses and fraudulent documents. The loss of foreign exchange to the country on this account was to the tune of Rs 2500 million. Prima facie, the transactions which were put through the South Indian Bank Ltd., Bombay, constituted offenses under the Foreign Exchange Regulation Act, 1973. The matter was, therefore, referred to the Foreign Exchange Enforcement Directorate, Bombay. Intelligence gathered by the Enforcement Directorate (ED), Bombay indicated that these activities were not limited to the South Indian Bank, but similar remittances were effected through other banks notably the United Commercial Bank, D.N. Road, Bombay.

In February 1996, Officers of the Enforcement Directorate conducted searches at a number of places and interrogated a large number of persons, including bank officials, who were arrested under the provisions of the Foreign Exchange Regulation Act, 1973. Investigations conducted so far revealed that remittances totaling US $ 160.94 million (equivalent to Rs. 5467.8 million), were effected through 12 different banks in Bombay, during the period 1991-1995. Broadly, the following modus operandi was followed : Persons involved in this racket, with the help of middlemen, recruited front persons for opening a number of accounts in the names of fictitious and non-existing firms. Large amounts of cash were deposited in these accounts and immediately after deposits were made, documents purportedly relating to goods imported into India by these firms were submitted to the banks concerned. On the basis of such documents the banks were effecting remittances favouring the "overseas suppliers" of goods. This modus operandi was used for flight of capital using official banking channels.

Investigations conducted so far revealed that the main persons involved in this racket are Dinesh C. Bhuva and Hemant Barot, who have been absconding ever since it came to light that they are the real brains behind the racket. However, a major breakthrough was achieved by the Enforcement Directorate when they succeeded in apprehending a member of this cartel - Harshad P. Mehta (not the Big Bull), whose interrogation provided numerous clues and vital information relating to this case. The money laundering syndicate headed by Dinesh C. Bhuva and Hemant Barot adopted the following techniques : Middlemen were employed to recruit persons :

- Of small means for opening bank accounts in the names of fictitious firms, for depositing cash and pay orders. These deposits were utilized for making remittances, against (fraudulent) documents covering imports.
- For depositing cash or pay orders obtained from other banks.
- For maintaining proper liaison with bank officials, to ensure that the transactions were conducted smoothly.
- Specialised in preparing forged documents, viz., Bills of Entry, Packing lists, Invoices, Customs duty paying documents and other related documents like Bills of lading, Insurance, etc. to cover fictitious imports.
- For contacting financiers who could lend money to the racketeers.
- For opening bank accounts in places like Hong Kong for receiving foreign exchange remittances from India. All the bank papers, including signed cheque books, were taken over in advance from those persons for withdrawal of foreign exchange remitted from the Indian banks to these accounts.
- To sell foreign exchange so obtained in Hong Kong to gold smugglers, exporters (who need foreign exchange for meeting their requirements of over-invoiced exports), importers (who need foreign exchange to meet their requirements of under-invoiced imports), and others who need foreign currency for various purposes. One of the precautions that was taken in all these transactions was to conceal the identity of the top hierarchy of the cartel and for this purpose, only middlemen were used for all transactions and for locating people who would open bank accounts in India and abroad, for depositing cash and pay orders, for obtaining fictitious documents to show that imports have been effected into India and for maintaining liaison with the bank officials. Nearly 33 persons have been arrested during the period February '96 to June' 96.

Conclusion: This case study clearly indicates as to how a criminal syndicate can set up within a short span a well organized apparatus for money laundering without revealing the identity of the top racketeers. It also indicates as to how the banking system is vulnerable to such operations and how the banking staff can be subverted. It is therefore necessary to emphasize the importance of implementing the recommendations of the Financial Action Task Force (FATF), immediately and in particular to take up reasonable measures to obtain information about the true identity of the persons on whose behalf an account is being opened or transactions are being conducted. The financial institution should keep records on customer identification. It is also necessary to observe due diligence and pay special attention to all complex and unusually large transactions which have no apparent economic or visible or lawful purpose. Suspicious transactions must be reported to the

Competent Authorities to investigate whether the financial institutions are being used as conduits for money laundering operations.

1. What is money laundering? Briefly explain the Prevention of Money Laundering Act, 2002. **(CO3)**

2. Describe the different methods of money laundering in India. How banks are used for money laundering? **(CO4)**

3. What is trade based money laundering? How is money laundering being done through foreign trade? **(CO4)**

4. What are the available measures in India by RBI and Government? What do you suggest to control money laundering in general and in trade transactions? **(CO2)**

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Section A

Answer all the questions **10 X 3 = 30 Marks**

1. What is gold exchange standard? **(CO1)**
2. What are the two plans were taken up at the Bretton Woods Conference in July 1944 and explain briefly. **(CO1)**
3. Brief the uses of SDR. **(CO2)**
4. Briefly explain the absorption approach to the BOP in exchange rate determination? **(CO2)**
5. Brief the risks associated to the trade. **(CO4)**
6. What is quantitative easing? **(CO1)**
7. What is law of one price? **(CO1)**
8. What is 'J' curve effect of Marshall-Lerner? **(CO1)**
9. Compare FEMA with FERA. **(CO2)**
10. Brief the prevention of money laundering act, 2002. **(CO3)**

Section B

Answer any three questions **3 X 15 = 45 Marks**

1. Explain the different types of transaction in the forex market. **(CO3)**
2. What is Triffin Dilemma? How it led to the reform measures in international financial system? **(CO1)**
3. Discuss the case for and against the IMF as an International Lender of last resort. **(CO2)**
4. What are objectives of FEMA? How the foreign exchange moves out of the country and moves in to the country through trade based money laundering practices? **(CO3)**

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