



# The Supreme Court on constitutionality and interpretation of provisions of the Prevention of Money Laundering Act, 2002

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## 1 Background

On 27 July 2022, a three-judge Bench of the Supreme Court of India delivered an important judgement in *Vijay Madanlal Chowdhary & Ors. v Union of India & Ors.* (**Vijay Madanlal**), in relation to key provisions of the Prevention of Money Laundering Act, 2002 (**PMLA**). The PMLA is India's principal anti-money-laundering statute, enacted to prevent money laundering and also provide for the confiscation of property derived or obtained as a result of criminal activity.

The PMLA came into force in 2005. Since then, it has been amended several times to bring it in line with international conventions relating to money laundering, particularly in response to recommendations made by the Financial Action Task Force. Significant amendments were recently made to the PMLA by the Finance Act, 2018 (**2018 Amendment**) and the Finance (No. 2) Act, 2019 (**2019 Amendment**) (together, the **Amendments**).

In *Vijay Madanlal*, the Petitioners (across over 200 petitions) had essentially challenged the constitutional validity of various provisions of the PMLA relating to the scope of powers vested in the Enforcement Directorate (**ED**), the investigating agency which is tasked with enforcing the provisions of the PMLA, and the Special Courts/Adjudicating Authorities which deal with the prosecution of offenders and the taking of possession/confiscation of properties.

The Supreme Court upheld the constitutional validity of the provisions under challenge. In doing so, it also expounded on several controversial issues relating to the construct of the offence of '*money-laundering*', the extent of investigative powers exercisable by the ED, the circumstances under which properties can be attached, and the conditions for grant of bail— all of which may be of particular relevance to companies or individuals who are or may be subject to investigation/prosecution under the PMLA.

## 2 Analysing key aspects of the judgement

### 2.1 What constitutes an offence of 'money-laundering'?

Section 3 of the PMLA, which defines the offence of '*money-laundering*', stipulates that "*Whosoever directly or indirectly attempts to indulge or knowingly assists or knowingly is a party or is actually involved in any process or activity connected with proceeds of crime including its concealment, possession, acquisition or use and projecting or claiming it as untainted property shall be guilty of offence of money-laundering.*" Subsequently, by way of the 2019 Amendment, an explanation (**Explanation I**) was added to Section 3 of the PMLA stipulating that Section 3 refers to the '*process or activity*' connected with proceeds of crime, namely: (a) concealment; or (b) possession; or (c) acquisition; or (d) use; or (e) projecting as untainted property or (f) claiming as untainted property.

In a landmark judgement, the Supreme Court expounded on several key issues relating to the construct of the offence of 'money-laundering', the extent of investigative powers exercisable by the Enforcement Directorate, the circumstances under which properties can be attached, and the conditions for grant of bail under the Prevention of Money Laundering Act, 2002.

The scope and ambit of Section 3 of the PMLA came into question following the 2019 Amendment on account of what appeared to be a discrepancy between Explanation I (which stipulated a person could be proceeded against for mere acts of concealment, possession, acquisition or use of proceeds of crime), and the main text of Section 3, which appeared to stipulate that an additional element of '*projecting*', or '*claiming*' proceeds of crime as untainted property was necessary to constitute an offence of money laundering.

The Petitioners relied on a previous judgement of the Supreme Court in *Nikesh Tarachand Shah v Union of India & Anr.*, and unsuccessfully argued that before somebody can be adjudged guilty of the offence of money laundering, the said person must not only be involved in any '*process or activity*' (such as concealment, possession, acquisition, or use) connected with proceeds of crime, but must also project or claim the proceeds of crime as being untainted property; and an interpretation to the contrary would result in enlarging the ambit of the main provision of a statute by way of an explanation that was inserted pursuant to an amendment, which would be unconstitutional. The Supreme Court in *Vijay Madanlal* observed that the interpretation of the Petitioners would "*undermine the efficacy*" of the legislative intent behind Section 3, which even prior to the amendment, was widely worded such that the explanation was only clarificatory. The earlier interpretation of the Supreme Court in *Nikesh Tarachand Shah* was therefore disregarded by the bench in *Vijay Madanlal*, and it was concluded that the '*process or activity*' can be in any form, whether it be one of concealment, possession, acquisition, use, or projection of the proceeds of crime as untainted property or claiming it to be so.

The question of what constitutes '*proceeds of crime*' had been dealt with by various High Courts in the past, albeit with inconsistent conclusions being reached. '*Proceeds of crime*' under Section 2(1)(u) of the PMLA includes property derived or obtained (directly or indirectly) as a result of criminal activity relating to a '*scheduled offence*', as specified in Part A, Part B and Part C of the Schedule to the PMLA. The Supreme Court, in *Vijay Madanlal*, clarified that all properties that are simply connected with or related to a scheduled offence will not constitute '*proceeds of crime*', unless such property is derived "*as a result*" of criminal activity related to a scheduled offence. It has further clarified that '*proceeds of crime*' can also be "*indirectly*" derived property, namely, property derived or obtained from sale proceeds or, in a given case, in lieu of or in exchange of the '*property*' which had been directly derived or obtained as a result of criminal activity relating to a scheduled offence.

This may become of particular concern to third parties such as a transferee, lessee, mortgagee, hypothecatee, manager, agent and trustee of property, who may have acquired a *bona fide* interest in a property, which was '*proceeds of crime*' in the hands of the transferor. Such property is susceptible to attachment/confiscation proceedings under the PMLA. This may also lead to financial institutions/creditors taking recovery action and additional challenges in securing interest in property perceived to be '*proceeds of crime*'. In fact, the Supreme Court was expressly conscious that the interpretation of Section 3 and the definition of '*proceeds of crime*' enunciated by it may lead to harassment of innocent persons who may unknowingly deal with persons who have committed the offence of money laundering and entered into transactions with them. The Court however considered that the concerns in this regard had to be overlooked to give effect to the objective of the PMLA of being a "*preventive Act*" and not simply a "*money laundering (penal) Act*."

## 2.2 Necessity of a predicate offence for proceedings against 'money-laundering'

As discussed above, an offence of money laundering relates to a process or activity connected with proceeds of crime (i.e., property derived or obtained as a result of criminal activity) relating to a scheduled offence, commonly called a '*predicate offence*'. An important issue that courts in India were confronted with in several

cases recently was whether under the PMLA, persons/properties can be proceeded against *de hors* a predicate offence; or in other words, whether the predicate offence ceasing to exist by virtue of acquittal or quashing would lead to the proceedings under the PMLA being rendered infructuous. While some High Courts and the Supreme Court (in its previous decisions) had taken the position that a predicate offence is an essential condition for proceeding under the PMLA,<sup>1</sup> others such as the Bombay High Court, most recently, took the view that the ultimate result of the investigation of the predicate offence (even if it results in closure of the case) cannot have a bearing on the proceedings under the PMLA which will continue on its own.<sup>2</sup>

In *Vijay Madanlal*, the Supreme Court rightly provided much-needed clarity on this issue by holding that if there is an acquittal/discharge of the accused or the accused is absolved from the predicate offence, then all proceedings under the PMLA in relation to such person or property ought to be closed.

### 2.3 Powers of the Enforcement Directorate relating to attachment, search and seizure

The Supreme Court in *Vijay Madanlal* also dealt with the question of whether the ED can commence proceedings under the PMLA independently and in the absence of a case being registered by the police (or other authority concerned) for a connected predicate offence. Specifically, the Court considered the exercise of the ED's investigatory powers of search and seizure under Section 17 of the PMLA, and attachment of properties under Section 5 of the PMLA.

In this context, the Supreme Court clarified that to initiate '*prosecution*' for an offence of money laundering, the registration of a complaint/report in relation to a predicate offence is a prerequisite, but for initiating actions of '*provisional attachment*' under Section 5 or conducting searches/seizures under Section 17 of the PMLA, there need not be a pre-registered criminal case in connection with a predicate offence. The Court held that for proceeding with provisional attachment, or search and seizure of properties, it is sufficient if the ED is satisfied (with reasons recorded in writing) that the accused concerned is in possession of '*proceeds of crime*'. Additionally, for exercising powers of provisional attachment, the ED must also be convinced that such proceeds of crime are likely to be concealed, transferred or dealt with in a manner which is likely to frustrate proceedings under the PMLA.

In this regard, the Supreme Court observed that if during an investigation, the ED discovers any questionable/undisclosed property, and the scheduled offence that it was obtained through is not already registered, it is open to the ED to still proceed to provisionally attach the property while contemporaneously sending information to the jurisdictional police for registering a case in respect of the scheduled offence. If the jurisdictional police "*fail to respond appropriately*" to such information, the authorised officer under the PMLA can "*take recourse to appropriate remedy, as may be permissible in law to ensure that the culprits do not go un-punished and the proceeds of crime are secured and dealt with as per the dispensation provided for in PMLA.*"

Accordingly, the Supreme Court's verdict strengthens the hands of the ED, as the agency is at liberty to attach assets and carry out raids even prior to the registration of a case relating to the predicate offence. In effect, the ED has been empowered to independently assess (at least at the stage of attachment/search and seizure) criminal activity relating to a scheduled offence, which otherwise falls within the realm of the jurisdictional police or other authorities empowered to investigate such scheduled offences.

<sup>1</sup> *P. Chidambaram v Directorate of Enforcement*, (2019) 9 SCC 24; *Prakash Industries v Directorate of Enforcement*, 2002 SCC Online Del 2087

<sup>2</sup> *Babulal Verma and Ors. v Enforcement Directorate and Ors.*, 2021 SCC OnLine Bom 392.

## 2.4 Right of accused to be informed of the grounds for arrest/attachment

In terms of generally applicable criminal procedures in India such as the Code of Criminal Procedure, 1973 (CrPC), an investigating officer is required to formally register a case in the form of a First Information Report (FIR) prior to commencing an investigation or arresting the accused. The FIR records allegations/information concerning the commission of an offence, and the accused, as a matter of right, is entitled to a copy of the FIR. The PMLA, on the other hand, does not statutorily prescribe a formal report to be registered for a case being investigated by the ED. However, in practice, ED officers maintain a record of a case in the form of an Enforcement Case Information Report (ECIR).

Given the absence of a statutory prescription for an ECIR, the Petitioners before the Supreme Court raised the concern that while some ED officers supply an accused with a copy of the ECIR, others do not. The Petitioners argued that the ED should be required to disclose the ECIR to an accused prior to arrest, as it contains the grounds of arrest, details of offences, etc., and not being provided with a copy would hamper an accused's ability to seek bail, and perhaps also defend himself at trial. The Petitioners argued that non-provision of the ECIR would therefore be a gross violation of an accused's fundamental rights under Articles 21 (the fundamental right to liberty) and 22(1) (the right of a person who is arrested to be informed as soon as may be about the grounds for his arrest) of the Constitution.

The Supreme Court rejected these arguments and held that an ECIR prepared by the ED is an internal document created by the ED rather than a statutory document. It is therefore not on the same footing as an FIR under the CrPC and is not required to be provided to an accused. Additionally, the Court held that there is no need to formally register an ECIR before attaching or confiscating property which is thought to be proceeds of crime under the PMLA, as these are civil actions.

Accordingly, the Supreme Court held that if the accused has been "*informed about the grounds*" of his arrest, that is sufficient compliance with the mandate of Article 22(1), and non-supply of the ECIR, which is essentially an internal document, cannot be cited as a violation of fundamental rights of the accused.

However, the judgement leaves several key questions unanswered, including the method by which the accused is to be informed of the grounds of his arrest i.e., whether the information is to be provided in writing, or oral intimation would be considered sufficient. Additionally, the level of detail the ED is required to give the accused regarding the offence is unclear, i.e., whether the ED is required to make the accused aware of the facts discovered during the investigation that support the accusation, or is simply required to inform the accused of the offence(s) he is being arrested for.

## 2.5 Powers to summon and punish for giving false statements

The Petitioners also challenged the constitutionality of Section 50 of the PMLA, which empowers the ED to summon any person to record his statement during investigation. The PMLA mandates that the person summoned is bound to answer the questions put to him truthfully and to produce the documents required by the officer, failing which he can be prosecuted under Section 63 of the PMLA. The Petitioners argued that this provision puts the ED in a position of being able to compel a person to make an incriminating statement against himself under threat of legal action, thereby violating the fundamental right against self-incrimination under Article 20(3) of the Constitution (which provides that no person accused of an offence shall be compelled to be a witness (i.e., give evidence) against himself).

The Supreme Court dismissed these arguments, upholding the validity of Section 50 on the basis that the protection of Article 20(3) only applies when the person summoned has been formally accused of an offence.

The Court noted that under Section 50, the summons may be issued in connection with an inquiry regarding proceeds of crime which may have been provisionally attached. This is not in the nature of an investigation for prosecution, and at this stage there would neither be a formal accusation against the person summoned, nor a formal document indicative of the likelihood of involvement of such person as an accused in the offence of money laundering. Moreover, the Court considered that the role of the ED at that stage cannot be equated with that of a 'police officer'. However, the Court clarified that if a statement is recorded after a formal arrest of an accused by the ED, then the protections against '*testimonial compulsion*' may come into play and "*that such statement, being in the nature of a confession, shall not be proved against him.*"

However, the Court also observed that if any statement is made by the person summoned which reveals the offence of money-laundering or the existence of proceeds of crime, then this may form the basis for further proceedings under the PMLA which could include prosecution of the individual concerned for the offence of money-laundering.

Section 50 of the PMLA, and the Supreme Court's observations in this regard, are contrary to generally applicable criminal law principles which stipulate that neither a witness nor accused is bound to answer questions which would have the tendency to expose such person to a criminal charge or penalty. Further, such statements, if at all, can only be used for the purposes of proving a contradiction between the testimony in court and the earlier statement given by the witness to the police.

The Supreme Court's observations regarding post-arrest protections against self-incrimination may be rendered illusory as a person who is summoned under Section 50 is vulnerable to be proceeded against and prosecuted based on statements that he may have been compelled to make. A person receiving summons may not have any visibility into the scope of allegations or issues under investigation by the ED, as the Court also held that the ED is not required to disclose the ECIR or other details of the investigation to the person summoned for questioning and therefore it's possible that a person summoned may make self-incriminating statements.

## 2.6 Conditions for grant of bail under the PMLA

Under the CrPC, a court dealing with a bail application filed by an accused is required to consider some of the following factors while deciding whether to grant or reject bail:

- the nature of the accusation and the severity of punishment in case of conviction;
- reasonable apprehension of witnesses tampering by the accused or the apprehension of threat to the complainant;
- the nature of supporting evidence for the purpose of recording a *prima facie* satisfaction of the court in support of the charge;
- the likelihood of the offence being repeated; and
- danger of the accused absconding or fleeing if released on bail.

However, Section 45(1) of the PMLA imposes two additional pre-conditions (**Twin Conditions**) for bail under the PMLA: (i) the public prosecutor has been given an opportunity to oppose the bail application; and (ii) the Court is satisfied that reasonable grounds exist for believing that the person is '*not guilty*' of the offence under the PMLA, and the person is not likely to commit any offence while on bail. Section 45(2) makes it explicitly clear that the conditions imposed by Section 45(1) apply in addition to the limitations under the CrPC and any other applicable law on granting of bail.

Prior to the 2018 Amendment, the Twin Conditions were applicable only when a person was accused of a predicate offence punishable with imprisonment for 3 years and above under Part A of the Schedule to the PMLA. This was struck down by the Supreme Court in its previous decision of *Nikesh Tarachand Shah*, on the ground that it was violative of the fundamental right to equality and the right to life and personal liberty under the Constitution. The decision was based on the reasoning that (i) the application of the Twin Conditions to only offences punishable for a term of imprisonment of more than three years under Part A of the Schedule to the PMLA was arbitrary and also resulted in an anomalous situation where a person was being prosecuted for an offence under the PMLA, but he was also being denied bail under the Twin Conditions based on the nature of the underlying predicate offence; and (ii) the Twin Conditions reversed the presumption of innocence, by mandating a court to determine whether the accused is 'not guilty' of the offence, and required the accused to disclose its defence at the stage of arrest itself, which was unjust and unfair.

By way of the 2018 Amendment, the Twin Conditions were made applicable to all offences under the PMLA, to alter the basis of the judgement in *Nikesh Tarachand Shah*. However, there remained a considerable divergence of opinion among various High Courts on whether the 2018 Amendment had the effect of resurrecting the applicability of the Twin Conditions, with many accused under the PMLA able to obtain bail even after the 2018 Amendment was passed based on only the conditions in the CrPC.<sup>3</sup>

In *Vijay Madanlal*, the Supreme Court upheld the Twin Conditions imposed by Section 45(1) as being reasonable and having a direct nexus with the purpose and objects sought to be achieved by the PMLA (i.e., to combat the menace of money laundering). The Court also clarified that the conditions imposed by Section 45 would be equally applicable to the grant of anticipatory bail for offences under the PMLA.

Consequently, persons accused under the PMLA will now find it significantly more difficult to obtain bail, as they will be required to convince a court that, based on the probability of the material collected in the ED investigation, they are 'not guilty' of the offence of money-laundering. Given the Supreme Court's findings in relation to the non-mandatory nature of an ECIR (as explained above) it can be expected that in some cases, this may also need to be done without having a copy of the ECIR or even knowing the nature of allegations made against the arrested individual.

### 3 Concluding remarks

Besides the issues discussed above, the judgement in *Vijay Madanlal* also deals with various other provisions under the PMLA concerning powers of the special courts and adjudicating authorities established under the PMLA to try money laundering offences and burden of proof in relation to proceeds of crime.

While the Supreme Court has overall emphasised and bolstered the intention of the legislature to prevent money laundering in the greater interest of the society as a whole, the judgement gives a lot of leeway to the ED to conduct investigations. With the Supreme Court upholding the stringent conditions of the PMLA thereby setting apart the PMLA from, and disapplying the safeguards provided by, generally applicable criminal law provisions, including the protection against self-incrimination and the presumption of innocence when deciding bail applications, the ED has heavy responsibility to conduct itself in line with the objectives/legislative intent that found favour with the Supreme Court.

<sup>3</sup> Kerala High Court in *M Sivasankar v Union of India*, 2021 SCC OnLine Ker 395 which held that the 2018 Amendment had resurrected the Twin Conditions. On the other hand, the High Courts of Bombay (in *Sameer Bhujbal v Directorate of Enforcement*, Bail Application No. 286 of 2018, decided on 06.06.2018) and Madhya Pradesh (in *Vinod Bhandari v Directorate of Enforcement*, 2018 SCC OnLine MP 1559) have held that the 2018 Amendment did not have the effect of resurrecting the Twin Conditions.

## ANALYSIS

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In addition to questioning the constitutional validity of various provisions of the PMLA as they currently stand, the Petitioners had also sought to challenge the Amendments on the ground that the manner in which the Amendments were brought into force was unconstitutional. This challenge has however been left to the determination of a larger bench of the Supreme Court comprising 7 judges. We await the decision of the larger bench on this question because if the manner in which the Amendments were introduced is held to be unconstitutional and the Amendments struck down, it would have a consequential impact on the findings in Vijay Madanlal (such as the expanded definition of money laundering, the widened definition of proceeds of crime, the stricter conditions of bail and the expanded list of offences which the ED can investigate) being negated as well. Additionally, if the Amendments are struck down by the larger bench, it may impact several ongoing investigations and trials, given that the Supreme Court in Vijay Madanlal directed that the amended provisions of the PMLA will have to be given effect until a judgement is rendered by the larger bench of the Supreme Court.

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