

The background of the journal cover features a top-down view of a desk. On the left, a pair of black leather brogue shoes is partially visible. In the center, an open notebook with lined pages and a silver pen lies on a light-colored wooden surface. To the right, a black leather bag with a zipper is partially shown, and a black leather watch with a silver dial is resting on the desk. A large, semi-transparent white rectangular box is centered over the image, containing the journal's title and ISSN information.

INTERNATIONAL LAW  
JOURNAL

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**WHITE BLACK  
LEGAL LAW  
JOURNAL**  
**ISSN: 2581-  
8503**

*Peer - Reviewed & Refereed Journal*

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# **SHELL COMPANIES AND ECONOMIC OFFENCES: ENFORCEMENT, JUDICIAL TRENDS & REGULATORY GAPS IN INDIA**

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## **Abstract**

Shell companies have become one of the most commonly used tools for economic wrongdoing in India. These entities, often created with no real business, exist to serve as masks. They hide the people who truly control them, fabricate expenses, move profits on paper, and help dirty money appear clean. Their misuse has contributed to large-scale tax evasion and increasingly complex financial crime, making them a persistent problem for enforcement agencies.

The study examines not only how shell companies are formed, but how they are manipulated to mislead systems designed to trust corporate forms. It looks at their role in falsifying financial records, misreporting taxable income, and layering illegal funds.

Through a doctrinal review, supported by an analysis of judicial decisions and policy frameworks, the research traces how courts deal with lifting the corporate veil, attaching assets, reassessment of income, and imposing corporate penalties. The case-law study indicates increasing judicial recognition; however, outcomes often depend on the strength of investigative evidence and the way liability is framed under different statutes.

The research identifies recurring real-world barriers faced by agencies and prosecutors: unclear or missing beneficial-ownership details, limited inter-agency coordination, difficulties in establishing mens rea, and procedural delays that weaken the fear of consequences. On the regulatory side, the study highlights that India still lacks real-time information sharing, strong cross-border disclosure powers, and full integration of digital-forensic and financial-tracking technologies that could expose these companies.

By connecting legal doctrine, judicial trends, and enforcement realities, this work aims to contribute to the discourse on financial regulation and law reform that tackles financial crime at its source to ensure that the corporate form, a legitimate engine for economic growth, is not misused as a vehicle for financial crime.

## Meaning and nature of Shell Companies

The term shell companies has gained increasing relevance in modern business and financial discourse, especially in the cases of economic crime. Although corporate entities are usually formed to conduct business that is legitimate, some structures like shell companies fall under a special category within the Corporate framework/ These entities, although they are legally formed, may not have actual business; this is where the question of whether they are being used properly arises.

*Black's Law Dictionary defines a shell company as "a firm that does not trade, is formed to raise funds, attempt the take-over, go public or act as the front for an illegal venture." Similarly, many double tax avoidance agreements (DTAAs) define shell companies to curb treaty abuse.*

Meanwhile, one should be able to differentiate between legitimate and illegitimate shell companies. Fraud is not the motive behind all shell companies. They are in most instances employed in lawful business practices, especially when it comes to complicated financial transactions. The issue is that when such entities are applied to cover illegal activities or avoid regulatory attention, this leads to the problem.

Finally, it is impossible to perceive the sense and the character of shell companies in terms of pure negativity. Although they have features that contribute to their abuse, they are also used in valid purposes in the corporate system. It is necessary to have a balanced understanding of these entities to analyse their contribution to economic offences and to have them well-regulated to respond effectively.

The Registrar is empowered under section 248 of the Act<sup>1</sup>, the Registrar has the power to approach the issue of dealing with shell companies. Change of Names of Companies Chapter XVIII of the Companies Act, 2013 (the 2013 Act) which includes Sections 248 to 252 of the Companies Act, 2013 (enforced w.e.f. 26 December 2016) has been comprehensively provided. Although the issue of removal of a company was covered in a single section i.e., section 560 of the Companies Act, 1956 (the 1956 Act), they are contained in five sections (section 248 to section 252) of the 2013 Act. Section 248 provides that in situations where the registrar has reasonable cause to suspect that a company is non-operational or non-compliant. This includes cases where the company has not started doing business within one year of incorporation, received the subscription amount from its subscribers or where the company has not filed the necessary declaration within the stipulated period.

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<sup>1</sup> Companies Act 2013, s 248

A company can also be struck off upon failure to conduct any business or activity during two financial years, without seeking dormant status. Also, in cases where physical verification indicates that the company is not undertaking any business or when statutory requirements in Section 10A are not met, action can be taken.

In such cases, the Registrar must provide a notice to the company and the directors and allow them to make a response within thirty days before the company's dissolution.<sup>2</sup>

The Calcutta High Court of U.N. Mandal Estate Private Ltd. held that the company was not operating because its directors and shareholders never sat together, its list of members and its returns, balance sheet and bank accounts were never filed, and its properties were never dealt with, sold and transferred. The court shall reinstate a company only when it is satisfied that: (a) the applicant was a creditor or contributory on the date of dissolution; (b) the company is solvent, and (c) the company was carrying out business on the date of striking off. 1 The MCA has also been utilising Section 164(2) of the Act in its quest to prosecute sham companies. Section 164 (2) states:

*“No person who is or has been a director of the company which- (a) has not filed financial statements or annual returns for any continuous period of three financial. shall be eligible to be re-appointed as a director of that company or appointed in other company for a period of five years from the date on which the said company fails to do so”<sup>3</sup>*

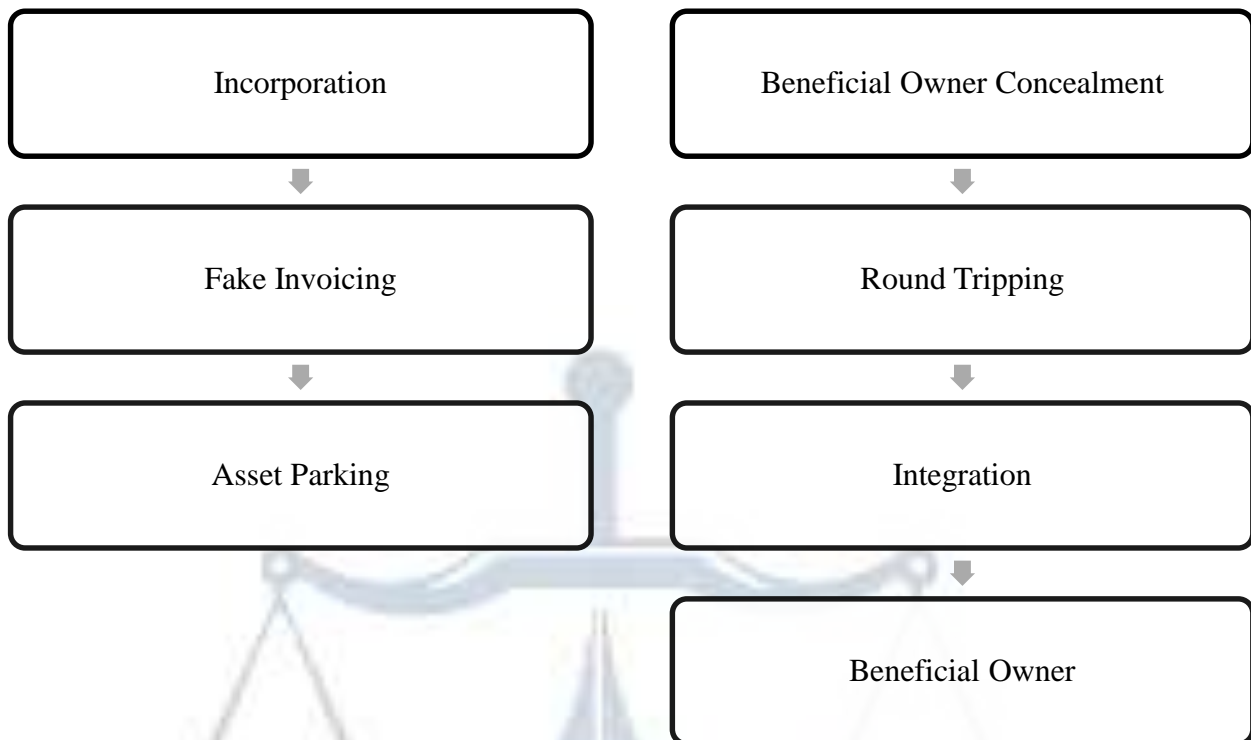
### **Working of shell companies:**

The functioning of shell companies is best understood by examining how they are structured and used in financial transactions

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<sup>2</sup> A Ramaiya: Guide to The Companies Act [Box 1], 19th ed, Vol 3 A Ramaiya Sudipto Sarkar and Arvind P Datar (Chief Editors) in collaboration with Specialist Editors

<sup>3</sup> AIR 1959 Cal 493



*Fig1.1*

### **1. Incorporation:**

The initial part of the operationalisation of a shell company is to incorporate it as a legitimate-looking legal entity. A private limited company can be incorporated using the SPICe+ form on the MCA21 portal<sup>4</sup> with minimum requirements, as mandated by the Companies (Amendment) Act 2013 - a proposed company name, a registered office address, at least two directors with Director Identification Numbers (DINs), a memorandum and articles of association, and a minimum paid-up capital. This ease of registration, intended to facilitate entrepreneurship, is systematically abused to create dormant companies with no actual business purpose. Shell companies use nominee directors, who lend their names to filings in the company but have no real control, to keep the semblance of a legitimate company, and the company is kept in the register indefinitely as long as it does not actually operate its business.

To keep the facade of legitimacy, shell companies use nominee directors - people who lend their names to the company filings in exchange for a fee but have no actual control over the company.<sup>5</sup> A common registered address, usually a CA office or a small shop used by dozens

<sup>4</sup> Ministry of Corporate Affairs, 'SPICe+ Form: Simplified Proforma for Incorporating Company Electronically' (MCA, Government of India, 2020) (<https://www.phdcci.in/wp-content/uploads/2021/11/MCA-inaugurates-SPICe-web-form-and-notifies-Companies-Incorporation-Amendment-Rules-2020-1.pdf>)

<sup>5</sup>FATF, *Misuse of Corporate Vehicles Including Trusts and Company Service Providers* (FATF 2006) 18–22. (<https://www.fatf-gafi.org/content/dam/fatf->

of companies at the same time, fulfils the requirement under Section 12 of the Companies Act 2013 without being automatically checked by the MCA.<sup>6</sup>

### **Concealment of beneficial ownership:**

After incorporation, the shell company is then employed to break the apparent connection between the assets or transactions and the actual person in control, the beneficial owner. This is accomplished by means of layered ownership: an Indian shell company can be owned by an offshore company in Mauritius or the British Virgin Islands, which is also owned by a trust in the Cayman Islands. A notable illustration of the functioning of shell or intermediary entities in complex financial structures can be seen in the *Tiger Global LLC* investment. In this Flipkart case, the company went through a multilayer offshore structure where Tiger Global LLC's capital was pooled through entities in Cayman and Mauritius. The Mauritius entities (Tiger Global II, III AND IV Holding) invested in Flipkart Singapore, which derives most of its capital from Flipkart India. The exit happened through the sale of shares of the Singapore entity as part of Walmart's acquisition of Flipkart. The Mauritius entities claimed that the capital gain from this sale was not taxable in India under the India-Mauritius Tax treaty<sup>7</sup>

Although the disclosure of significant beneficial ownership is now required by Section 90 of the Companies Act 2013,<sup>8</sup> and is often complied with in form only, once incorporated, the shell company is used to sever the apparent connection between the assets or transactions and the actual controlling person - the beneficial owner. This is done via layered ownership; an Indian shell company can be owned by an offshore company in Mauritius or the British Virgin Islands, which is again owned by a trust in the Cayman Islands. Although Section 90 of the Companies Act 2013 now requires disclosure of significant beneficial ownership, this is often a fiction or incomplete, and offshore layers are hard to lift without mutual legal support.

This has been long-established in the experience of enforcing financial action plans by the Financial Action Task Force, which has identified the abuse of legal persons, especially dormant companies with nominee directors, as one of the key gaps in global anti-money laundering regimes.<sup>9</sup> This has also been confirmed by the experience of India: the 2017 crackdown by the Ministry of Corporate Affairs struck off more than 2.26 lakh companies.

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[gafi/reports/Misuse%20of%20Corporate%20Vehicles%20including%20Trusts%20and%20Company%20Services%20Providers.pdf.coredownload.inline.pdf](#)

<sup>6</sup> Companies Act 2013, s 12

<sup>7</sup> 2026 INSC 60 (THE AUTHORITY FOR ADVANCE RULINGS (INCOME TAX) AND OTHERS V/S TIGER GLOBAL INTERNATIONAL II HOLDINGS )

<sup>8</sup> Companies Act 2013, s 90; Ministry of Corporate Affairs, General Circular No. 07/2023 (MCA 2023).

<sup>9</sup> FATF, Guidance on Beneficial Ownership for Legal Persons (FATF 2023)

This has been identified by the Financial Action Task Force as the most significant weakness in the global anti-money laundering systems: the misuse of legal persons, specifically dormant companies with nominee directors, has been mentioned since 2013.

### **Mechanisms of Fund movement:**

Using the corporate structure, the shell companies make it easy to transfer illicit money using a number of intersecting methods:

Fake Invoicing is one of the most widespread is fake invoicing. Within the GST regime, this allows the shell company to claim invoices of services not rendered - consulting, software development, royalties - against an actual business, allowing the money to be laundered while creating a paper trail that appears transactional despite no actual transaction occurring.<sup>10</sup>

Round-tripping is a second major technique, particularly involving offshore shells. Money out of India is brought back as payments to a foreign company - to license a brand, pay management fees, or freight - and is brought back as Foreign Direct Investment or External Commercial Borrowings, now a legitimate source of foreign capital.<sup>11</sup>

Asset parking shell companies allows beneficial owners to hold property like real estate, equity stakes, intellectual property in the company's name rather than their own. When a regulatory scrutiny falls on the individual, the assets do not appear in their personal name. Under the Prevention of Money Laundering Act 2002, the Enforcement Directorate may attach such property as proceeds of crime under Section 8,<sup>12</sup> but this requires first establishing the predicate offence and tracing the ownership chain — a process complicated by layered structures.

Integration and the problem of legitimacy.

Integration is the last phase of money laundering process, whereby the laundered money is introduced back to the economy in the form of legitimate income. This is the point at which the crime money is camouflaged as legitimate income via loan repayments by affiliated organizations, returns on investments or wages paid through shell companies. The importance of this step has been noted by the Supreme Court in the case of *Vijay Madanlal Choudhary v Union of India* when the Court mentioned the money laundering process including such stages as the placement, layering and integration. This underscores the relevance of the shell firms in enabling the ultimate legitimisation of the illicit money in the legitimate financial system.

*37. ....Section 3 of the 2002 Act, the same defines the offence of money-laundering. The*

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<sup>10</sup> Central Goods and Services Tax Act 2017, s 16;

<sup>11</sup> Reserve Bank of India, Report on Foreign Exchange Management (RBI 2018) .

<sup>12</sup> Prevention of Money Laundering Act 2002, s 8

*expression "money-laundering" ordinarily means the process or activity of placement, layering, and finally integrating the tainted property in the formal economy of the country. However, Section 3 has a wider reach. The offence, as defined, captures every process and activity in dealing with the proceeds of crime, directly or indirectly, and not limited to the happening of the final act of integration of tainted property in the formal economy to constitute an act of money-laundering.*<sup>13</sup>

At this point, the burden of each transaction can be corroborated by documentation, such as loan agreements, board resolutions, valuation reports, and so on, and the entire scheme is challenging to prosecute.

The Supreme Court has acknowledged this in the case of *Nikesh Tarachand Shah v Union of India* which highlights the evidentiary challenges in the context of PMLA prosecutions, and it underlies the contested burden-of-proof provision under Section 24 of the Act, which shifts the onus onto the accused to prove that proceeds are untainted<sup>14</sup>

The inherent issue with the regulation of shell company activities is that the Indian company law has traditionally been biased to separate registration and verification of economic substance. The MCA registers, but does not certify that the entities are actually doing business. Detection is left to the Enforcement Directorate, the Serious Fraud Investigation Office and the Income Tax Department, which detect the fraud after the event, often many years later, and thus the lack of integrated real-time data sharing between the MCA, GST Network and banking regulators.

### **Role in Economic Offences**

Shell companies are not just a corporate anomaly, but they are in fact tools of economic crime. This part discusses the main groups of economic crimes that shell companies enable in the Indian setting, the enforcement statistics that highlight their magnitude, and the law that characterises and criminalizes such practices.

Money laundering: Perhaps the most well-identified purpose for using shell companies in India is to commit the act of money laundering, that is, making illegal gains appear legal through some sort of financial transaction. The offence under Section 3 of the Prevention of Money Laundering Act, 2002 can be stated as anyone who indulges either directly or indirectly with any proceeds of crime. <sup>15</sup>Shell companies are used to carry out all the steps of this process:

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<sup>13</sup> (2022) SCC Online SC 929

<sup>14</sup> (2018) 11 SCC 1, [45]

<sup>15</sup> Prevention of Money Laundering Act 2002, s 3.

placement by receiving illicit funds, layering by means of inter-company transfers and false invoicing, and integration in PMLA cases. The Enforcement Directorate applied its powers to attach assets of over 99,356 crore between 2014 and 2022 in PMLA cases, a large percentage of which were associated with shell company networks.<sup>16</sup> Cases like - *The Rose Valley Real Estate and Construction Ltd v State of West Bengal*<sup>17</sup> chit fund fraud and the Punjab National Bank scam involving Nirav Modi<sup>18</sup>— revealed elaborate shell company structures spanning multiple jurisdictions used to layer and conceal proceeds of fraud

Tax evasion: The shell companies are at the core of the tax evasion mechanism in India and they work through their mechanisms by taking advantage of the loopholes between the process of corporate registration and substantive verification. These are some of them that are directly tackled in the ITA 1961. Section 68 treats unexplained cash credits in company books as income subject to tax,<sup>19</sup> Whilst Section 56(2) taxes receipts of less than adequate consideration, both of which are routinely used to avoid transactions involving shell companies<sup>20</sup>.

The 2016 exercise of demonetisation radically revealed the shell company tax evasion role. A post-demonetisation analysis by the Income Tax Department revealed that more than 35,000 shell companies deposited about ₹17,000 crore of invalidated currency in a few weeks following the announcement, turning black money into bank deposits through fake share allotments and unsecured loans. The implementation of GST in 2017, aimed at providing a single and traceable record of transactions, also provided a new avenue to commit tax fraud. Networks of fake invoices, in which shell companies issue invoices over non-existent supplies, so that they can claim fraudulent input tax credit, have been noted as a major burden on enforcement. The CGST Act 2017, in Section 16, limits ITC to genuine supplies and in Section 122 penalties are imposed in case of issuing false invoices, but the invoice data has to be cross-matched on the GST Network, which will lag significantly behind the fraud.<sup>21</sup>

Fraud and misappropriation of funds in the company: In addition to money laundering and tax evasion, shell companies are also frequently used to engage in corporate fraud - the diversion of funds of legitimate companies to shells associated with those shells in favour of promoters. The Companies Act 2013 has introduced certain provisions to deal with this. Section 447 defines fraud in broad terms, encompassing any act with the intent to deceive, and prescribes

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<sup>16</sup> FATF, Misuse of Corporate Vehicles Including Trusts and Company Service Providers (FATF 2006)

<sup>17</sup> (2019) SCC Online Cal 1132

<sup>18</sup> Central Bureau of Investigation, *Case Details: Nirav Modi-PNB Fraud* (CBI 2018)

<sup>19</sup> Income Tax Act 1961, ss 68

<sup>20</sup> Income Tax Act 1961, ss 56

<sup>21</sup> Central Goods and Services Tax Act 2017, ss 16, 122; Central Board of Indirect Taxes and Customs, Circular No. 171/03/2022-GST (CBIC 2022) 3

imprisonment of up to 10 years along with a fine. <sup>22</sup>Section 212 empowers the SFIO to investigate companies where fraud is suspected, including powers of search, seizures, and arrest.<sup>23</sup>

The IL&FS collapse of 2018 demonstrated how shell company structures within a supposedly regulated group could hide the true financial position of its entities to both auditors, regulators and creditors at the same time. It was also revealed in the SFIO investigation reports in both cases that over 200 companies, many of which were shells, were used to launder investor deposits into real estate and media assets controlled by the<sup>24</sup>

Hawala and cross-border value transfer: Shell companies also overlap with hawala networks - informal systems of value transfer that are not part of the banking system. Although hawala does not necessarily involve any corporate set-up, shell companies serve as the formal level on which hawala proceeds are legitimised. <sup>25</sup>The Foreign Exchange Management Act 1999 bans unauthorised cross-border capital flows in Section 4<sup>26</sup>, Violations are punishable by the Reserve Bank of India, but require identification of the underlying transaction, which shell company layering is designed to avoid.

The importance of shell companies, specifically in Indian economic offences, is that they serve as infrastructure, and not as separate tools. The experience of the Enforcement Directorate has demonstrated that the cases of major economic offences will often involve shell company networks where one shell company is used by different principals or where related companies use hundreds of shells at various phases of the same scheme.

## Conclusion

Shell companies hold a legally grey but economically important status in the corporate system. As this paper will show, they are not necessarily illegal entities; they can be as legitimate as the purpose of their use. Although they have legitimate functions in the structuring of investments, facilitating complex transactions, and allowing corporations flexibility, their very nature, low disclosure, easy incorporation and the ability of layered ownership, make them especially vulnerable to abuse as a tool in economic crimes.

Their operation analysis shows that shell companies are often deployed to conceal the

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<sup>22</sup> Companies Act 2013, s 447

<sup>23</sup> Companies Act 2013, s 212.

<sup>24</sup> SFIO, Annual Report 2021–22 (Ministry of Corporate Affairs 2022)

<sup>25</sup> Financial Intelligence Unit – India, *Annual Report 2020–21* ([https://fiuindia.gov.in/pdfs/downloads/AnnualReport2020\\_21.pdf](https://fiuindia.gov.in/pdfs/downloads/AnnualReport2020_21.pdf))

<sup>26</sup> Foreign Exchange Management Act 1999, s 4;

beneficial ownership and create the transactions and transfer the funds between jurisdictions. The examples of fake invoicing, round-tripping, and asset parking show how these entities can give an illusion that they are legal when in reality they are funding illegal financial transactions. They play a particularly important role in the process of money laundering, during which they facilitate the steps of placement, layering, and integration and ultimately enable the process of bringing illegal money back into the formal economy in the guise of legitimate income.

The Indian judicial reaction is indicative of an increasing realization of these issues. Courts have started to embrace more the substance-over-form approach, citing things like lifting the veil of incorporation and the broader perspective of financial crimes under statutes such as the Prevention of Money Laundering Act, 2002. But the success of judicial intervention usually lies in the presence of specific evidence and the capacity of the enforcement agencies to follow intricate financial paths. Consequently, results are still random, especially in situations that involve multi-layered structures as well as cross-border structures.

One of the major problems that are revealed in this research is the structural loophole between the registration of corporations and the verification by the regulations. The Indian legal system has also contributed to the ease of doing business by simplifying incorporation procedures, but has inadvertently led to the creation of non-operational or fraudulent entities. Regulatory control is mainly reactive in nature compared to the presence of detected suspicious activity, as a result of which regulatory control is imposed. This lag greatly undermines the deterrent impact of enforcement and makes the process of asset recovery more difficult.

Moreover, the presence of persistent challenges, including the inadequacy of the disclosure of beneficial ownership, lack of coordination between the regulatory bodies, as well as limited technological integration, makes the proper monitoring challenging. The lack of real-time data transmission among the institutions such as the MCA, GST Network, and banking regulators creates the gaps that can be utilized by the shell company networks. Moreover, cross-border investigations can be limited by jurisdictional constraints and dependence on international mechanisms of co-operation, which can be cumbersome or ineffective.

Finally, the problem of shell companies cannot be resolved by the ban only. In its turn, it needs a well-tuned regulatory reaction that strikes the balance between economic flexibility and accountability. The reinforcement of positive ownership structures, increasing inter-agency coordination, and use of technology to track financial transactions in real time are important measures toward alleviating abuse. Finally, the need to ensure that the corporate form is not used as a tool of illegal actions is not only necessary to ensure the integrity of the financial system but also to maintain confidence in the corporate governance and economic institutions.