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Theoretical foundations of money laundering and terror financing: conceptual analysis of legal frameworks and global challenges

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Abstract

Money laundering (ML) and terrorism financing (TF) remain major threats to the financial stability of the global financial system. These illicit activities exploit transnational networks and take advantage of the interconnectedness of an increasingly globalized world. While international framework models were adapted in the form of conventions, treaties, recommendations, and directives, the gap between the theoretical model and its actual application remains significant, particularly in less-developed countries (LDCs). These problems are aggravated by globalization, which makes complex transnational financial crimes easy. This study critically examines global instruments, such as the Vienna, Palermo, and Merida Conventions. I employ doctrinal legal research and a legal narrative analysis method to explore how these frameworks address the challenges posed by transnational financial crimes. The results indicate considerable variation in term implementation, especially in LDCs, where limited resources and institutional capacity erode international Anti-Money Laundering (AML) and Counter-Terrorism Financing (CTF) progress. Moreover, financially motivated crimes are constantly evolving, and advancements and regulatory loopholes outpace the existing enforcement mechanisms. Moreover, this study demonstrates that a harmonized approach integrating legal and financial perspectives is essential for effectively combating ML and TF. This study highlights the importance of strong international cooperation, consistent legal standards, and technological tools. This study addresses the gap between theory and practice, supporting the formulation of adaptive policies regarding AML and CTF that increase resilience to transnational financial crimes. The implications of these findings for global policymaking are significant, and they provide a roadmap for reconciling international frameworks and mechanisms in domestic framing and policing. More needs to clarify the refinement of risk-based approaches, enhancement of regulatory compliance in LDCs, and promotion of collaborative networks between states to counter dynamic threats posed by ML and TF in the future.

Keywords: Economic Crime, AML/CFT Regulations, TOC, Globalization

Jel codes: K00, K42, F52, O17, K33

1. Introduction

Money laundering (ML) and terrorism financing (TF) severely threaten global financial stability and security, escalating through the connectedness of financial systems of globalization, as this integration fosters transnational crimes, enabling financial misconduct to expand across borders. Transnational crimes weaken governance structures, threaten systemic risk, and other illicit activities, such as drug running and arms smuggling. For instance, according to AML Intelligence Correspondents (2024), more than \$3 trillion in illicit funds flowed through the global financial system in 2023, despite the global legal framework for Anti-Money Laundering (AML) and Counter-Terrorism Financing (CTF), which is structured through internationally recognized instruments, including United Nations (UN) conventions, which codify binding obligations for states; the Financial Action Task Force (FATF) recommendations, which establish risk-based standards for compliance;



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and European Union (EU) directives, which operationalize these norms into enforceable national legislation. The persistent evolution of financial crimes highlights a critical disconnect between theoretical frameworks and their practical applications, particularly in less-developed countries (LDCs). This study addresses these challenges through the lens of globalization and explores its relationship with regulatory measures and crime network adaptability.

Utilizing a doctrinal legal approach and legal narrative analysis, this study reviews relevant international treaties, domestic laws, and literature in the field that create conceptual support for AML and CTF architecture. Critical analysis is also provided for foundational instruments such as the FATF Recommendations, the UN Convention, treaties, and the EU's Anti-Money Laundering Directives (AMLD). These include inconsistent compliance, resource limitations, and the lagging nature of modern regulatory frameworks to the rise of emerging technologies such as digital transactions and decentralized finance (Defi). The findings stress that the disproportionate vulnerabilities of LDCs are weak regulation and low institutional capacity enforcement, leaving fertile grounds for financial crimes. Drawing from key theoretical concepts, including the ML stages and crime-terror nexus, this study highlights how globalization acts as a driver of change in both the nature of crime and the enforcement approaches deployed to combat it. This study highlights the challenges of reconciling national regulatory frameworks at the global level and draws attention to the need for contextualized approaches to address the specific needs of LDCs.

This study aimed to achieve the following three goals: - First, I analyze the theoretical and legal foundations supporting the current AML and CTF architecture. Second, I address the needs and viability of the current frameworks. Finally, I work towards a solution that connects the realms of law, financial regulation, and emergent technology. At the heart of the exploration are questions about whether current legal principles are adequate, whether global coordination mechanisms are effective, and what forms of reform may be necessary to facilitate enforcement and promote adaptability. The significance of this study lies in its potential to inform both academic discourse and policy making. By addressing the disconnect between theory and practice, this study contributes to the development of robust and globally harmonized AML and CTF strategies. This emphasizes the need for interdisciplinary approaches that bridge legal, financial, and technological perspectives to combat the dynamic threats of transnational financial crimes.

2. Literature review

2.1. Overview

ML and TF pose systemic threats to the global financial integrity, national security, and economic sovereignty. These crimes exploit deregulated markets and interconnected financial infrastructure, transcending national boundaries to destabilize countries, irrespective of their developmental status. The post-9/11 era formed TF's dual economic-security ramifications, galvanizing international efforts to disrupt illicit financial networks. However, the mutual relationship between ML and TF, wherein both crimes leverage identical banking channels, shell corporations, and informal value systems, complicates regulatory variation and enforcement (Freyer, 2008). Further globalization exacerbates these challenges by eroding jurisdictional sovereignty and enabling criminal networks to exploit regulatory asymmetries and fragmented governance frameworks.

As Honga et al. (2025) explained, while ML seeks to legitimize proceeds from predicate offenses, such as drug trafficking or corruption, TF operationalizes resources for ideological violence, irrespective of fund origins.

This distinction necessitates divergent policy response. ML demands forensic financial tracing of severe crime-terror nexuses, whereas TF requires intelligence-driven asset freezing to dismantle terror ecosystems. Jakobi (2018) observed that financial globalization facilitates capital mobility but also creates vulnerabilities exploited by criminal networks. The United Nations Convention against Transnational Organized Crime (Palermo Convention 2000), underscores this duality, recognizing ML's role in perpetuating organized crime while framing TF as a threat to international peace. These developments necessitate adaptive regulatory frameworks that align with the evolving nature of financial crime (Tosza, 2024).

According to Fabre (2005), the financial crisis provided fertile grounds for ML operations to expand and evolve. The economic scale of these crimes remains staggering and is estimated to account for 2–5% of global GDP, translating to \$800 billion to \$2 trillion annually. Moiseienko (2023) argued that these illicit economies sustain transnational threats, ranging from narcotic cartels to insurgencies, creating feedback loops that crumble state institutions and distort legitimate markets. Addressing these issues between ML and TF, as both crimes leverage similar networks and financial systems, challenges detection and enforcement mechanisms.

The FATF remains the cornerstone of transnational AML and CTF governance; however, its soft law recommendations face uneven adoption, particularly in jurisdictions with weak institutions or competing political priorities. According to Tosza (2024), LDCs often lack the technical capacity to implement FATF's

risk-based approach, inadvertently creating safe havens for illicit finance. However, Scholars critique this regime's reliance on voluntary compliance, noting the absence of binding mechanisms to penalize state actors complicit in ML and TF networks (Ismaeel, 2024). Furthermore, the FATF's "naming and shaming" methodology risks alienating states that require capacity-building support rather than punitive measures.

By bridging the doctrinal gaps between economic focus ML gain and security dimensions of TF issues, policymakers can develop adaptive strategies that prioritize intelligence-sharing, cross-jurisdictional litigation protocols, and institutional resilience against regulatory capture. Such syntheses of theory and practice remain critical for safeguarding global financial systems while preserving the equitable development aspirations enshrined in international law.

2.2. Theoretical and conceptual foundations of ML and TF

The theoretical and conceptual foundations of ML and TF explore their evolution within the broader framework of transnational organized crime (TOC). These financial crimes exploit the uncertainty and fluidity of global networks and continuously adapt to technological and economic shifts. The literature highlights the dual influence of globalization, enabling cross-border criminal operations while also necessitating international regulatory responses.

Scholars have characterized the "glocal" nature of ML and TF, referring to their local origins and global expansion (Hobbs, 2001). As highlighted by Vander Beken and Janssens (2015), these crimes often emerge in regions with universal corruption and weak governance, thus reinforcing the complexity of their regulations. Addressing these issues requires an integrative legal approach that acknowledges both the local realities and global enforcement mechanisms.

A. Theoretical perspectives and analysis

i. Transnational organized crime (TOC) and ML/TF: The rise of globalization has transformed the landscape of financial crime, embedding ML and TF within the broader context of TOC. The Palermo Convention of 2000 defined transnational crime as acts committed by structured groups across national borders for financial or material gain. Scholars highlight that this broad conceptualization reflects the fluidity and adaptability of modern criminal networks (Lazarus, 2024). However, Tatulli (2024) argues that this definition lacks specificity, particularly in distinguishing between hierarchical criminal organizations; for example, the Italian mafia's global expansion was rooted in local influence, enabling the group to extend its operations across borders. By contrast, emerging decentralized cybercriminal networks exploit digital anonymity to circumvent traditional legal frameworks (Nguyen & Luong, 2021). This distinction is crucial for understanding differential regulatory responses. Despite the foundational contributions of the Palermo Convention of 2000 and the FATF, significant gaps remain in bridging global frameworks with local realities. Jakobi, A. P. (2015) argued that The FATF encounters significant challenges in global governance, particularly in launching effective initiatives and maintaining long-term commitment. Emerging theoretical perspectives advocate a more integrative approach that combines legal, socio-economic, and technological dimensions to address the complexities of ML and TF.

ii. Balancing compliance and enforcement: Theoretical frameworks addressing ML and TF largely focus on financial transparency and international regulatory standardization. FATF played a pivotal role in shaping global AML and CTF frameworks. However, according to Obokata (2010), these international standards prioritize formal compliance over substantive enforcement, particularly in jurisdictions with limited institutional capacity. Regulatory challenges have been further exacerbated by the rise of digital financial systems, which enable anonymous and rapid cross-border transactions, thereby exposing gaps in the existing legal frameworks (Tsingou, 2005). Emerging theoretical perspectives call for a multidimensional approach that integrates the legal, socioeconomic, and technological dimensions to effectively combat ML and TF. For example, Shelley (2003) highlights that ML not only enables financial crime, but also contributes to systemic instability and governance failures. Krylova (2024) provides a comprehensive analysis of the intersection of human trafficking, and ML illustrates how criminal networks exploit regulatory weaknesses and perpetuate corruption, economic inequality, and financial insecurity.

iii. Objectives of AML/CFT legal frameworks: The primary objectives of the AML and CFT legal frameworks are as follows: 1. Prevent the misuse of financial systems for illicit activities (Khan, Jani, and Zulkifli, 2021), 2. Protect financial institutions from being exploited for criminal purposes (Pavlidis, 2021), and 3. Enhance global security by disrupting financial crime networks (Romaniuk, Kaunert, and Fabe, 2023). These legal frameworks aim to detect, deter, and disrupt financial crimes through preventive mechanisms, legal penalties, and international co-operation. The core aspects of these frameworks are listed in Table 1.

Table 1. Key categories and measures of AML and CFT laws

Category	Key Measures
Prevention & Detection	<p>Financial institutions implement protocols to verify customer identities and monitor transactions (FATF– R.10 and UNTOC-Art.7 – Requires states to implement CDD and KYC protocols.).</p> <p>Asset Freezing/Seizure: Legal authority to restrict and confiscate illicit assets (UNSCR-1267 and 1373 / FATF-R.4).</p> <p>Global Standards Adoption: Alignment with FATF Recommendations to strengthen preventive frameworks (FATF-Rs.40, specifically Rs.1-5, 10-16, 24-25, and 35 and UNCAC-Art.14).</p>
Legal Enforcement & Penalties	<p>Criminalization of ML/TF: Codification of offenses with penalties including imprisonment and fines (UNTOC, Article 6; UNSCR 1373, Para. 1(b); FATF Recommendation 3).</p> <p>Autonomous Offenses: Distinct legal treatment of ML and TF to enable specialized prosecution (ICSFT, 1999, Article 2; EU AMLD 6, Article 3; FATF R.5).</p> <p>Specialized Agencies: National bodies (United Nations Convention Against Corruption (UNCAC), Article 36 – Calls for the establishment of specialized national law enforcement agencies to investigate ML offenses.</p> <p>FATF R.30 – Requires states to establish financial intelligence units (FIUs) and law enforcement bodies dedicated to investigating ML/TF</p>
International Cooperation	<p>Cross-Border Collaboration: Joint investigations, intelligence sharing, and legal assistance treaties (UNTOC, Article 18; UNCAC, Articles 46-48; FATF R.36).</p> <p>Compliance Monitoring: Regular FATF mutual evaluations to address jurisdictional gaps (FATF R.40; FATF Mutual Evaluation Process, 2021; IMF/World Bank AML Assessments).</p>

Source: Author's own construction based on key AML and CFT laws

These laws are designed not only to punish offenders, but also to prevent the misuse of the global financial system for criminal purposes. Legal scholars such as Rotman, E. (2021) emphasized that the challenge of combating financial crime is deeply tied to the increasing globalization of financial markets and the complexity of cross-border illicit activities. The internationalization of financial crime necessitates the creation of a legal architecture that can transcend national borders, creating a harmonized legal approach to both regulation and enforcement.

iv. Globalization and jurisdictional challenges: AML and CTF laws strive to address the global nature of ML and TF by promoting international cooperation through mechanisms such as Mutual Legal Assistance Treaties (MLATs) and extradition agreements. However, their effectiveness often depends on political will and institutional capacity (Obokata, 2010). The increase in DeFi further complicates AML enforcement. Scholars have highlighted how crypto-based financial systems enable anonymous and instantaneous transactions, making it difficult to track illicit funds (Shelley, 2003; Tsingou, 2005). While the FATF's Travel Rule addresses some risks, enforcement remains constrained by technological and jurisdictional limitations. A more integrative legal approach that incorporates socioeconomic reforms, digital innovations, and cross-border collaboration is needed to ensure the long-term effectiveness of AML and CTF regulations.

B. Conceptual perspective and analysis

ML and TF operate within a highly interconnected financial ecosystem that exploits the regulatory and economic loopholes. While ML aims to conceal illicitly obtained funds (Clarke, 2022). TF directs financial resources towards ideological or political objectives, rather than profit. This duality creates reverse laundering effect whereby legitimate funds are redirected into illicit activities, demonstrating an operational overlap between the two crimes (Krieger and Meierrieks, 2011). The mutuality of ML and TF highlights the need for a sophisticated regulatory approach to combat evolving methodologies.

i. The relationship between ML/TF: The overlap between ML and TF is evident in historical cases where criminal organizations and terrorist networks have co-opted similar financial mechanisms to sustain their activities. For instance, The Drug Enforcement Administration (DEA, 1990) exposed Operation Polar Cap, a landmark U.S. law enforcement initiative revealed, how the Medellín cartel laundered \$1.2 billion through U.S. financial institutions using trade-based laundering and shell companies. Similarly, according to Shelley (2014), Hezbollah's financial operations leveraged narcotic trafficking and gold mining to finance its activities, reinforcing the operational convergence of ML and TF. This interplay is particularly pronounced in weak governance environments where ineffective regulatory frameworks and institutional corruption enable the proliferation of financial crime. The absence of stringent AML and CFT controls in developing regions exacerbates vulnerability, allowing criminal enterprises to integrate illicit funds into legitimate financial systems with minimal detection risk.

ii. The stages and methods of ML/TF: ML operates through a structured process comprising three stages. In the first stage, illicit funds are introduced into the financial system, the placement of which often involves cash-intensive businesses or structured deposits to evade reporting thresholds. For instance, Canadian studies reveal that 46.3% of offenders use high-cash businesses such as car dealerships to facilitate structured transactions (Schneider, 2020). The second stage is layering, which is a complex transaction that obscures the origins of illicit funds and often utilizes offshore accounts, shell corporations, and digital assets. A key example is Operation Green Ice, where the Cali cartel funneled \$50 million across multiple jurisdictions (Farer, 1999), effectively disguising the illicit nature of funds. The final stage is Integration, at this stage Laundered funds re-enter the economy through legitimate assets and business ventures, often in real estate or luxury markets. Pablo Escobar's property acquisitions exemplify this stage, where criminal proceeds are blended seamlessly with legal wealth (Rajbhandari, 2022), which complicates asset recovery efforts.

Parallel to ML, terrorist financing networks exploit similar methodologies, but with distinct end goals. Similarly, Maimbo (2004) highlighted that Hawala systems and informal value transfer mechanisms (IVTS) serve as prominent channels for anonymous cross-border transactions, often bypassing formal banking scrutiny. South Asian terrorist organizations have consistently leveraged Hawala networks, integrating proceeds from opiate production and trade-based laundering into operational funding (Durrani, Anwar, & Hussain, 2024).

iii. Understanding licit and illicit money and crime-terror nexus: The phenomenon of ML is far from victimless crime. Its scale, complexity, and ability to destabilize both financial systems and governments make it one of the most dangerous and pervasive threats to the global economy. Kaufmann and Kaliberda (1996) distinguish between non-criminal informal economic activities (e.g., tax evasion and unregistered businesses) and criminal activities (e.g., drug trafficking, financial fraud, and terrorism). The overlap between informal and illicit financial flows complicates enforcement efforts. For example, Lord Grabiner's (2000) findings on social welfare fraud in the UK demonstrate how illicit activities siphoned millions of public funds, reinforcing the blurred lines between fraud and legitimate financial practices. Van Duyn (2003) identified the scale of hidden economy in transition economies such as Bulgaria and Ukraine; the "gentrification of crime money" has led to the funneling of illicit wealth into legitimate enterprises. Masciandaro (2000) explained Tinbergen's Gravity Model (adapted for financial crime), suggesting that criminals prefer jurisdictions with robust financial infrastructure but weak AML enforcement, creating regulatory paradoxes in developed economies. Unger's (2007) research on financial

crime highlights that well-established financial systems in the U.S. and EU are prime destinations for laundered funds, challenging the perception that laundering is confined to tax havens.

In summary, financial crime and crime money operate within a complex nexus between the legitimate and illegitimate economies. Theoretical, empirical, and case-based insights underscore the need for comprehensive strategies that integrate international cooperation, robust enforcement, and technological innovation to mitigate the far-reaching impacts of financial crime.

2.3. Conceptualizing the global AML and CFT architecture

Global AML and CTF architectures have evolved into a complex interplay of binding treaties, soft law instruments, and multinational governance mechanisms, such as the UN Conventions and FATF Recommendations, providing the foundation for harmonized efforts against ML and TF. These frameworks define predicate offenses, regulate financial flows, and establish compliance standards to safeguard global financial systems (de Koker, 2024). According to Zagaris (2015), a key concept within these frameworks is "soft law," when applied in practice it means that norms are neither binding nor enforceable but persuasive, which enables the cross-border collaboration despite jurisdictional variance.

A. Foundational pillars of global AML/CFT regime

According to Nyreröd, Andreadakis, and Spagnolo (2023), The AML regime initially focused on drug trafficking before expanding into organized crime governance in the 1990s under the FATF and UN frameworks. Further the adoption of The Palermo Convention (2000) marked a turning point in consolidating AML measures within international law. The TF discourse gained prominence in 1999, yet only a few countries adopted its framework until post-9/11, when the CTF became a global security priority (Wesseling 2013). United state-led initiatives within the FATF introduced special recommendations in 2001, merging AML and CTF under a unified illicit finance framework encompassing both illicitly acquired wealth and funds used for illegal activities. The evolution of global AML and CFT strategies reflects a dynamic and multi-layered response to the increasing sophistication of financial crimes, such as ML and TF. As Ryder et al. (2023) highlights an effective AML strategy must integrate criminalization, preventive measures, enforcement mechanisms, and international cooperation to address the multifaceted challenges posed by these transnational crimes, which are deeply intertwined with globalization and cross-border illicit activities.

- i. *Criminalization and harmonization of ML/TF*: The criminalization and harmonization of AML and CFT laws are rooted in international legal instruments that establish binding obligations on states, while grappling with challenges in enforcement and jurisdictional consistency. The United Nations in 1988 shaped the United Nations Convention against Illicit Traffic in Narcotic Drugs and Psychotropic Substances, the Vienna Convention (1988), and after two years outlined the protocols for the United Nations Convention against Transnational Organized Crime (UNTOC), the Palermo Convention (2000) represents two cornerstone treaties that impose dual legal obligations: 1. explicit criminalization of ML and TF as autonomous offenses; and 2. Mandatory establishment of cross-border recovery and confiscation mechanisms. The Vienna Convention operationalizes these principles through Article 3, which defines ML as the conversion, transfer, or concealment of proceeds derived from drug-related crimes (Stessens 2000), The International Convention for the Suppression of the Financing of Terrorism (1999) expands the scope to include terrorist financing, mandating the freezing and confiscation of assets (Bantekas 2003). Similarly, Article 2 of the Palermo Convention (2000) extends these prohibitions to terrorism financing, reinforcing states' obligations to identify, seize, and repatriate illicit funds associated with organized crime and terrorist networks (United Nations, 2004). A summary of the legal framework for AML and CTF is presented in the following Table 2, which typically includes the key components and elements of legal instruments.

Table 2. Key components and elements of legal instruments.

Element	Key Legal Instruments	Key Elements
Criminalization	The Vienna Convention 1988	Defines money laundering (ML) as disguising proceeds from drug trafficking (Art. 3) Requires international cooperation for asset recovery.
	T. F Convention 1999	Mandates freezing assets linked to terrorism (Art. 2). Criminalizes terrorism financing (TF) as a standalone offense.
	The Palermo Convention 2000	Expands predicate offenses beyond drugs (Art. 6). Obliges state to criminalize ML as part of transnational crime networks.
Preventive Measures	FATF 40+9 Recommendations	Risk-Based Approach (RBA) for CDD/KYC (R.1). Virtual asset regulation (R.15), and Beneficial ownership transparency (R.24–25).
	EU AML Directives	A set of regulatory requirements issued by the European Union (EU) containing directives 1 to 6 to combat ML/TF by EU member states.
International Cooperation	FATF Mutual Legal Assistance (MLA)	Peer-review mechanisms (e.g., greylisting). Standardizes cross-border STR
	UN Security Council Resolution 1373 (2001)	Requires states to criminalize TF and deny safe havens Mandates asset freezes under Chapter VII authority

Source: Author's own construction adapted from key legal frameworks

In practice, the harmonization of AML and CFT laws requires a balance between stringent enforcement and jurisdictional flexibility, particularly in the context of financial innovation. The proliferation of DeFi platforms, which operate beyond traditional banking channels, has further exacerbated enforcement gaps, necessitating regulatory adaptations that align with FATF Recommendation 15 on Virtual Assets and Virtual Asset Service Providers (VASPs) (FATF, 2012, 2023).

ii. Soft law as adaptive governance: Soft law plays a vital role in fostering international harmonization. For example, Ebikake (2023) explored the role of soft law FATF's 40 + 9 recommendations in establishing a comprehensive framework to assist countries in addressing illicit financial activities. However, a few studies, such as Gazi (2024), have examined the FATF mutual evaluations 2023, which revealed stark disparities, as developed nations achieve high compliance with customer due diligence (CDD) rules, whereas LDCs average due to institutional resource gaps. This asymmetry enables jurisdictional arbitrage, and the use of shell companies contributes to financial secrecy and corruption risk (Shipley et al., 2023). However, a few works, such as Boister (2014), have examined the concept, and the voluntary nature of soft law presents challenges, as

varying levels of political will and institutional resources result in inconsistent compliance. For instance, less developed countries often fail to fully implement FATF standards, creating loopholes for financial crimes.

Soft law mechanisms, particularly those promulgated by the FATF, serve as critical instruments in fostering the international harmonization of AML and CFT laws, establishing a globally recognized regulatory framework, and offering guidance on risk-based compliance, CDD, and financial intelligence sharing (FATF, 2023). Unlike binding treaty obligations, soft law instruments rely on voluntary adoption and periodic peer reviews to ensure alignment across jurisdictions. However, the FATF (2023) mutual evaluations show considerable discrepancies in compliance. This asymmetry facilitates regulatory arbitrage, allowing illicit actors to exploit non-compliant jurisdictions for the creation and formation of shell company, trade-based money laundering (Ferwerda & Unger, 2023). Achieving efficient and successful harmonization necessitates strengthening compliance incentives, reinforcing accountability mechanisms, and integrating emerging financial technologies into the AML and CFT governance frameworks.

B. Key International Organizations and Actors

The global fight against ML and TF requires a coordinated and multilevel regulatory approach involving key international, regional, and national actors. These institutions have legal frameworks, enforcement mechanisms as well as intelligence sharing networks targeting the financial crimes that transcend national borders. However, Levi and Reuter (2020) highlight discrepancies in transposition and resource limitations in some jurisdictions, hindering their effectiveness. The complexity of this regulatory structure necessitates a critical examination of the functions key international bodies play in this, the evolution of legal frameworks, and the prevailing global trends shaping AML and CTF enforcement.

i. Multilateral Organizations: At the international level, the FATF, UN, International Monetary Fund (IMF), and World Bank have set AML and CTF standards, conduct evaluations, and provide technical assistance. Legal model of FATF operates using a risk-based approach, which puts the onus on states to adopt policies which take account of their own financial situations and institutional capabilities (Subramanian, 2016). However, in practice, the FATF exerts pressure on jurisdictions through its mutual evaluation process that assesses the level of implementation across member states. Countries that fail to meet compliance requirements face greylisting and blacklisting issues. Blacklists consist of high-risk countries and jurisdictions subject to stringent sanctions by the FATF, While Grey Lists identify jurisdictions with relatively less severe deficiencies in AML and CFT measures (Khouny & Drissi, 2025).

By adopting conventions and resolutions that create legally binding obligations for its member states, the UN has played an essential role in shaping the international frameworks for AML and CTF. Building upon this legal foundation, UN Security Council Resolution 1373 (2001) introduced detailed mechanisms for cutting off funds and information from terrorists, compromise both cross-border co-operation and intelligence sharing at greater expenses than ever before. Few studies have systematically outlined guidelines to improve the effectiveness of counter-financing measures. For example, Kao et al. (2023), have outlined good practices to enhance the effectiveness of counter-financing measures, however, the enforcement of the resolution has been uneven, as politically unstable jurisdictions often fail to align domestic laws with UN mandates.

In financial sector assessments and economic stability programs, the IMF and World Bank both incorporated AML and CTF measures. Despite the IMF's risk-based monitoring model tackling AML and CTF, particularly in economies identified as high-risk jurisdictions (Ferwerda, 2022). In contrast, the World Bank's focus has turned to capacity-building programs that supply technical assistance for poorer countries to revise their AML and CFT laws in line with international norms-presenting rare development challenges, for emerging economies (Azing, 2018).

ii. Regional AML/CTF Enforcement Bodies: Regional players, such as the EU, Asia-Pacific Group on Money Laundering (APG), and Caribbean Financial Action Task Force (CFATF), acquaint these global frameworks with regional contexts and to their own situations and tackle specific risks. The EU has institutionalized AML compliance through binding directives, requiring uniform implementation across member states. For example, Tosza and Voordeckers (2024), have analyzed the establishment of the Anti-Money Laundering Authority (AMLA) within EU-level enforcement authority, which marks a major transition towards centralized AML supervision. The AMLA will assume most of its tasks and powers from July 1, 2025, and direct supervision from its Frankfurt-based headquarters will commence as of 2028.

iii. National-level enforcement agencies: National Financial Intelligence Units (FIUs) serve as lead enforcers of AML and CTF regulations, responsible for analyzing suspicious transaction reports (STRs) and coordinating intelligence-sharing. The Egmont Group is a trans governmental network of Financial Intelligence Units (FIUs) dedicated to enhancing cross-border cooperation. Its primary objective is to facilitate the exchange of

information between FIUs, fostering stronger collaboration in the fight against financial crimes (Mouzakiti, 2020). Their core tasks as well as enforcement mechanisms have been summarized in Table 3.

Table 3. Summary of AML/CTF bodies and Their Roles

Level	Organization	Role	Enforcement Mechanism
Global	The FATF UN IMF World Bank Egmont Group of FIUs	Global standard-setting bodies for AML/CTF legal frameworks. Provides technical AML/CTF capacity-building for developing nations and facilitates global intelligence-sharing among FIUs	Greylisting & Blacklisting for non-compliant states; Peer reviews of AML/CTF measures and international AML/CTF investigations
Regional	EU-AMLD & AMLA APG CFATF GAFISUD	FATF-Style Regional Body (FSRB) implementing AML/CTF standards across member states	Implements peer reviews and regional training programs. Conducts regional compliance assessments and enforcement measures
National	National FIUs & Central Banks	Conduct STR analysis, support financial crime investigations, and coordinate compliance with FATF and regional directives. Analyze Suspicious Transaction Reports (STRs), investigate financial crime networks, and enforce AML laws	Work under Egmont Group framework for FIU collaboration and STR-sharing and Operate as independent national regulators, ensuring compliance with FATF and regional AML requirements

Source: author's own adaptation based on *key organizational structure and their role*

The international, regional, and national organizations play complex and multifaceted roles in the implementation and enforcement of AML and CTF laws demonstrated in Table 3 above.

2.4. Challenges and Limitations in Global AML and CFT Frameworks

The transnational nature of ML and TF requires a coordinated legal and operational framework. However, systemic challenges including jurisdictional conflicts, sovereignty disputes, and technological evolution undermine the efficacy of global AML and CFT regimes.

A. Jurisdictional and Sovereignty Barriers

i. Territorial Limitations vs. Transnational Crimes: Traditional territorial jurisdiction, while foundational to state sovereignty, fails to address cross-border financial crimes. Transnational ML and TF networks exploit legal fragmentation, particularly in LDCs with weak institutional capacity and systemic corruption. Sovereignty, a cornerstone of international law, poses significant hurdles as states prioritize non-interference in domestic affairs over international collaboration. Kan (2016) explores the intersection of international security, emphasizing its impact on geopolitical stability that the principle of sovereignty often leads to legal fragmentation, allowing criminals to exploit weak jurisdictions. Nieto Martín and Nieto Martín (2022) argue that Westphalian sovereignty conflicts with borderless financial crime, as transnational criminal activities challenge the traditional notions of territorial jurisdiction and punitive authority (*Ius Puniendi*). Similarly, Yun (2024) highlighted how China's Blockchain Service Network (2024), which mandates data localization, exemplifies how national policies obstruct cross-border investigations, further complicating transnational financial crime enforcement. While global frameworks, such as the Vienna Convention (1988) and the Palermo Convention (2000) offer

mechanisms for international cooperation, their enforcement remains inconsistent. Mugarura (2016) observed that developed nations with robust institutional frameworks can adapt these principles effectively, whereas LDCs struggle to align with global AML and CTF standards, creating gaps in enforcement and jurisdictional oversight.

ii. Sovereignty vs. Extraterritorial Enforcement: Extraterritorial jurisdiction—a mechanism for addressing transnational antecedents—extends a state’s legal authority beyond its territorial borders. This approach is justified by the need to protect the international financial system from criminal activity. However, Borlini (2017) argued that the extraterritorial enforcement of AML and CFT measures goes against state sovereignty, causing disputes over enforcement legitimacy and legal jurisdiction. This results in unilateral compliance burdens, for example under U.S. (FATCA/Patriot Act) and EU (AML directives) laws, which are often criticized as bilateral pieces of legislation undermining multilateral governance regimes. Despite their potential, extraterritorial measures often clash with state sovereignty. Chehtman (2010) highlighted how jurisdictional expansion beyond territorial limits raises fundamental legal and ethical concerns, particularly when powerful economies impose unilateral compliance obligations on foreign financial institutions. Consequently, while AML and CFT laws aim to create a standardized global compliance framework, their asymmetrical application fosters regulatory gaps that sophisticated criminal networks can exploit.

B. Enforcement Asymmetries and Global Coordination

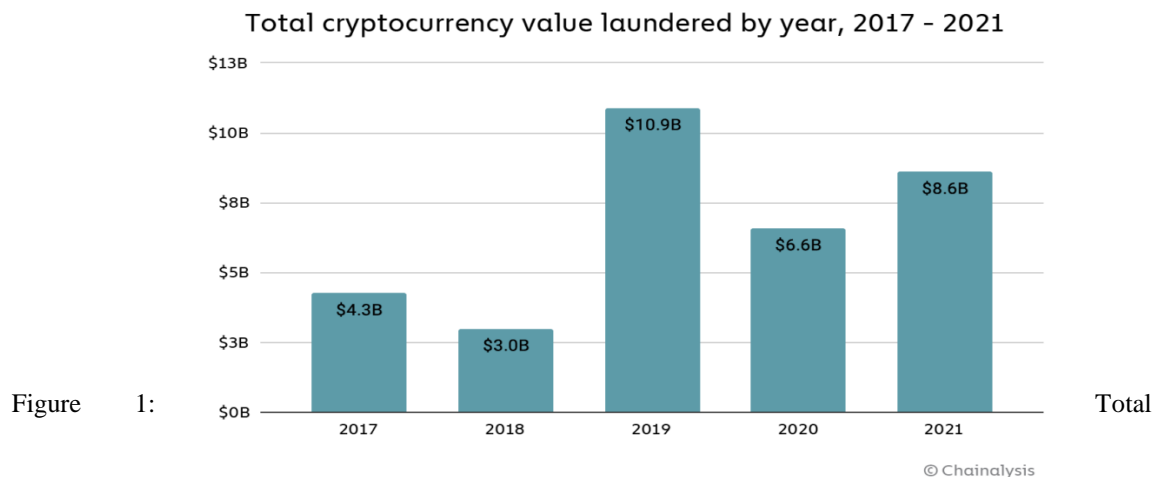
The strength of AML and CTF measures depends highly on international enforcement mechanisms such as mutual legal assistance, intelligence sharing and regulatory convergence. Mutual evaluation processes led by the FATF and other bodies, and compliance reviews, are critical to determining standards globally.

i. Disparities in Regulatory Capacity: The international AML and CTF regimes largely operate via soft-law instruments, especially the FATF recommendations, which, though widely supported, are not legally binding. Instead, they apply regulatory pressure by means of mutual evaluations, peer reviews and blacklisting of jurisdictions that fail to comply. Countries failing to meet FATF standards face economic repercussions, including restricted access to international financial markets (Beekarry, 2011). However, compliance varies across jurisdictions as geopolitical interests, institutional capacity, and financial incentives influence regulatory adoption, often leading to selective enforcement and regulatory gaps. This disparity in compliance creates an asymmetric regulatory landscape, where less-developed countries (LDCs) struggle with higher non-compliance rates due to resource constraints, weak institutional frameworks, and limited enforcement capabilities (Mugarura, 2017) compared to G20 nations.

ii. Institutional Contradictions: Financial institutions responsible for frontline AML and CFT compliance frequently prioritize commercial interests over strict regulatory adherence, balancing profitability with enforcement obligations (Stessens, 2000). Consequently, this regulatory misalignment is further exacerbated by the FATF’s punitive measures, which disproportionately impact jurisdictions with weaker institutional capacity while failing to address underlying structural deficiencies (de Koker, Howell, & Morris, 2023). Scholars highlight that existing enforcement mechanisms do not account for the capacity asymmetries between developed and developing nations, leading to unequal compliance burdens and economic disadvantages for financially weaker states (de Koker et al., 2023).

C. Technological Disruption and Illicit Finance

Global financial integration and technological advancements have amplified the complexity of combining ML with TF. The proliferation of digital payment systems, DeFi, and cryptocurrencies has created new avenues for illicit financial flow, with criminals exploiting pseudonymity, cross-border transaction capabilities, and regulatory gaps. In cases such as Binance, one of the world's largest cryptocurrency exchanges, reached a historic \$4.3 billion settlement with U.S. authorities for violations related to inadequate AML compliance, marking one of the largest penalties imposed in the sector (Binance, 2024). This case underscores the increasing regulatory scrutiny of cryptocurrency platforms and enforcement challenges in digital financial ecosystems (Binance, 2024). Liberland further underscores the challenges of the experimental crypto governance model, illustrating the risks of regulatory evasion, as it seeks to establish a decentralized financial ecosystem with minimal oversight (Crypto.ro, 2025). While the FATF promotes standardization in AML and CTF regulations, enforcement gaps across jurisdictions create opportunities for regulatory arbitrage, allowing illicit actors to engage in “forum shopping” to exploit less-regulated financial environments. The rise in cryptocurrencies and DeFi has intensified AML and CFT enforcement challenges, such as pseudonyms and cross-border transactions create regulatory blind spots. Chainalysis (2022) reported \$33 billion in laundered crypto assets between 2017 and 2021, with illicit flows peaking at \$10.9 billion in 2019 and \$8.6 billion in 2021 As shown in Figure 1. This trend aligns with the growing regulatory concerns highlighted in cases like Binance’s \$4.3 billion settlement, where authorities struggle to enforce compliance in decentralized financial ecosystems (Binance, 2024).



cryptocurrency value laundered by year, 2017–2021 (Chainalysis, 2022).

Source: Chainalysis Team. (2022). DeFi Takes on Bigger Role in Money Laundering.

This trend highlights the increasing complexity of illicit financial activities in decentralized digital economies, where chain hopping and cross-asset swaps obscure transaction trails. Europol's 2025 intervention against a \$100 million crypto-laundering network underscores the vulnerabilities within DeFi, as mixers and cross-chain bridges facilitate layering strategies that hinder forensic tracing (BitDegree, 2025). These mechanisms enable the seamless obfuscation of illicit funds, reinforcing the urgent need for regulatory frameworks to address DeFi's evolving financial crime risks.

ii. Regulatory Adaptation: International efforts to mitigate technological vulnerabilities in AML and CFT enforcement, despite these challenges, have resulted in measurable progress. Evidence suggests that although emerging Financial Technology (FinTech) products increase the ML and TF risks due to the differential take-up of regulatory technologies (RegTech) in the long-term, ML and TF risk detection will improve significantly with the incorporation of AI engines (Wang, 2023). Studies demonstrate that such advancements reduce false positives by 40%, improving the efficiency in identifying suspicious transactions while strengthening compliance frameworks (Wang, 2023). For example, enabling organizations to improve their operations in spotting suspicious transactions while making their compliance frameworks more robust. In the case of ML, machine learning models have improved real-time surveillance of all the advanced ML techniques, such as structuring and micro-transaction layering, which are capable of evading conventional rule-based compliance systems (Ahmad & Gasmi, 2024). The integration of AI-driven transaction monitoring has strengthened risk assessment frameworks, improving accuracy detection, and adaptive regulatory responses to evolving financial crime threats (Silent Eight, 2024). In summary, while digital innovations introduce new vulnerabilities, synchronized international cooperation and AI-enhanced compliance mechanisms are essential for mitigating financial crime risks.

D. Pathways for Reform and Future Directions

i. Hybrid Jurisdictional Models: The global legal complexities of AML and CTF enforcement stem from jurisdictional conflicts, sovereignty concerns, and inconsistent regulatory applications. While international frameworks provide theoretical guidance, enforcement remains fragmented because of disparities in legal interpretivism and decentralized financial structures (Qiang, 2024). A hybrid jurisdictional approach integrating blockchain for regulatory transparency and AI-driven compliance could enhance enforcement while respecting sovereign legal frameworks (Pepito, 2024). Strengthening cross-border legal protocols and capacity-building initiatives for LDCs is essential for harmonizing global and local enforcement efforts.

ii. AI-Enhanced Coordination: Integrating blockchain analytics and machine learning into FATF mutual evaluations can address detection gaps while reducing compliance burdens. Future research must prioritize the development of hybrid jurisdictional models and innovative enforcement mechanisms to effectively counter the evolving dynamics of money laundering and terrorism financing. Contemporary scholarship identifies three persistent structural gaps: the tension between Westphalian sovereignty and transnational financial crime networks, the divergent implementation of FATF standards across jurisdictions (Verdugo Yepes, 2011); and

regulatory lag cryptographic assets and Defi financial engineering (FATF, 2021). These challenges underscore the limitations of state-centric enforcement models.

3. Discussion and Findings

The connected nature of ML and TF within the global financial system poses challenges to effective regulation and enforcement. The Vienna Convention (1988), the Palermo Convention (2000), and the Merida Convention (2003) provide the foundation for international legal frameworks addressing ML and TF, yet significant gaps remain. These conventions establish critical legal standards but reveal inconsistencies when confronted with the transnationality of financial crimes. For instance, Article 3 of the Vienna Convention mandates the criminalization of ML arising from drug trafficking. However, its enforcement is hindered by disparities in national implementation. Hoffer (1999) examined the extraterritorial enforcement of U.S. money laundering laws through Operation Casablanca, where financial institutions across the U.S. and Mexico facilitated ML due to weak compliance mechanisms in Mexico.

The Palermo Convention broadens the scope of predicate offenses to include all serious crimes (Article 18), emphasizing mutual legal assistance. However, enforcement remains uneven, particularly in regions with limited institutional capacities. A notable example is the *Litvinenko Assassination Case*, in which gaps in extradition frameworks under the Convention prevented key suspects from facing justice across jurisdictions, and van den Herik and Anstis (2025) examined transnational repression in the context of international law. Moreover, Articles 51 and 52 of the Merida Convention focus on anti-corruption, linking corrupt practices to ML, yet weak asset recovery frameworks undermine its goals, as scholars Obioma, Nwuzor, and Nwankwo (2024) discuss Nigeria's failure to repatriate over \$321 million in embezzled funds despite international cooperation.

i. Contradictions Between Theory and Enforcement: Although conventions provide a robust theoretical foundation, their implementation contradicts the reality of the ML and TF crimes. The lack of standardization in Criminal networks exploit legal inconsistencies, as demonstrated by *Danske Bank Scandal* (2018), where €200 billion in suspicious transactions flowed through Estonia, bypassing AML controls in multiple jurisdictions (Faccia, Moşteanu, Cavaliere, & Mataruna-Dos-Santos, 2020). Thus, extraterritoriality competes with these challenges. The U.S. Patriot Act (Section 319) extends U.S. jurisdiction over foreign financial institutions but has faced criticism for undermining sovereignty. For example, the *United States v. Bank of Nova Scotia* demonstrated how extraterritorial subpoenas conflicted with Canadian privacy laws, thereby creating dilemmas in diplomatic tension and compliance.

ii. Challenges of Globalization and Technology: Globalization and technology exacerbate ML and TF enforcement gaps. Criminals have leveraged DeFi and cryptocurrencies to evade detection. Spotlight, Europol (2021) explored the evolution of cryptocurrencies in criminal financial activities and the challenges in law enforcement tracing a complex investigation involving 20 countries that resulted in the dismantling of a criminal network laundering tens of millions of euros in stolen funds. The Vienna Convention, which was limited to physical assets, struggled to address virtual currency. Similarly, the FATF's Travel Rule (R.16), which requires cryptocurrency exchanges to share transactional data, remains inconsistently enforced across jurisdictions.

3.1. Findings

The findings reveal a critical disconnect between theoretical models and practical enforcement. Although the FATF Recommendations and international conventions provide a robust conceptual foundation, their application is hindered by jurisdictional disparities and resource constraints. This discussion underscores the inefficacy of the extradition and asset-freezing processes in uncooperative jurisdictions. Meanwhile, fragmented beneficial ownership registries allow criminals to obscure illicit funds, with Panama and Pandora Papers' revelations exposing the widespread misuse of secrecy jurisdictions.

Further reliance on punitive measures such as blacklisting has disproportionately affected LDCs without addressing the root causes of non-compliance. The repeated greylisting of nations such as Pakistan from 2008 to 2022 (Sultan, Mohamed, Said, & Mohd, 2024) demonstrates the cyclical nature of this approach, necessitating a shift toward capacity-building initiatives that enhance institutional resilience.

Future research should explore the integration of technological tools into enforcement strategies. Moreover, creating hybrid jurisdictional models that incorporate elements of sovereignty and international collaboration is necessary to harmonize the enforcement lacunae. Mutual Legal Assistance Treaties (MLATs), for example, could be redesigned to allow for real-time intelligence-sharing infrastructure to overcome the delays that present barriers to cross-border investigation.

4. Conclusion

This study underscores the importance of aligning theoretical and legal frameworks with the dynamic reality of transnational financial crimes. This study contributes to the development of more cohesive AML and CTF strategies by addressing the limitations of the existing instruments and proposing adaptive solutions. The findings highlight the need for interdisciplinary approaches that integrate legal, technological, and socioeconomic dimensions to enhance global financial security. Addressing these challenges requires a collective commitment to harmonize international standards with localized realities, fostering a coordinated response to the evolving threats of ML and TF.

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