

THE EUROPEAN UNION'S ANTI-MONEY LAUNDERING CRUSADE

– A Critical Analysis of the Responses by the EU/EC
to Money Laundering

JOHANNA PEURALA

Police College of Finland
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Johanna Peurala
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ACRONYMS

- AML – anti-money laundering
- AMLS – anti-money laundering strategy
- BCCI – Bank of Credit and Commerce International
- CDD – customer due diligence
- CFSP- common foreign and security policy
- EC – European Community
- EU – European Union
- GPML – Global Programme against Money Laundering
- FATF – Financial Action Task Force
- FIU – financial intelligence unit
- FORPAC – Fonds Provenant des Activités Criminelles
- IMF – International Monetary Fund
- KYC – know your customer
- OC – organised crime
- PEP – politically exposed person
- STR - suspicious transactions report
- UNODC – United Nations Office on Drugs and Crime
- WCO – World Customs Organisation

“There are few other examples in the history of mankind that so dramatically illustrate such concerted effort to denounce and discourage a practice which even a few years ago was neither understood nor for that matter necessarily considered improper.”¹

¹ B Rider, ‘Editorial’ (1997) 1(2) J.M.L.C. 116 cited in S Heikinheimo, *Rahanpesu, erityisesti kriminalisoinnin ja konfiskaation näkökulmasta* (Poliisiammattikorkeakoulun tutkimuksia 6 1999) 63

1 INTRODUCTION

“With the coming-together of the different societies we also have an approximation of senses of justice, which might lead one day to genuine European criminal law.”²

1.1 General

The European Union (EU) represents a unique form of intergovernmental co-operation. But this kind of a union with internal markets has also lot of challenges regarding the criminal activities which try to take advantage of the free market area of the union. Indeed the EU has regarded the dangers arising from organised crime (OC) being such that the Union should take some steps to minimise those dangers for its markets. Although the activities of OC are manifold, money laundering is regarded as an inherent part of those activities. By ensuring the confiscation of the proceeds gained from these illegal activities, the EU has tried to reduce the overall activities of OC.

In this piece of research the look is taken into the anti-money laundering strategy (AMLS) of the EU, evolution of it, the rationale behind it and the success of that strategy. But first the question, why did I choose this topic to my thesis, is posed.

The chose of the topic was made a step by step basis; firstly I wanted to examine the money laundering phenomenon and the rationale behind the criminalisation of money laundering but then I decided to bring along the measurements taken against it at the European level. And when most of the EU’s measures against money laundering have basis on some international conventions those conventions had also to be examined. I also wanted to look those EU measures in a larger context so they are seen in my piece of research as a part of the EU’s control policy and the all measurements taken at the EU/EC level are seen to build up a strategy which I will call in this dissertation as *‘European Unions Anti-Money Laundering Strategy’* (EU’s AMLS).

The EU’s AMLS can be seen as an example of the control policy approach of the EU using which the EU is seeking to harmonise some parts of substantial criminal laws of the Member States, the parts which the EU sees to be crucial to ensure the proper function of internal market and to prevent abuses of it and to tackle organised crime. The EU also tries to build up an *‘Area of Freedom, Security and Justice’* and that stresses the necessity to harmonise

² W Perron, *‘Perspectives of the Harmonisation of Criminal Law and Criminal Procedure in the EU’* in Husabö et all *Harmonization of Criminal Law in Europe* (Intersentia, Antwerpen 2005) 22

some of the contents of substantial criminal law. Money laundering, with its close relationship to OC, is among the fifteen areas³ of EC's particular interest because of its close relationship with the core EC interests, cross-border importance and political importance.

But this EU's anti-money laundering crusade⁴ has not been a piece of cake in any sense. First of all, the money laundering is a very complex and ever-changing phenomenon the scale of which cannot be exactly known. One can even argue that money laundering should not be regarded a culpable act at all. On the other hand, money laundering with its transnational nature is usually considered to be fatal to world wide economy by feeding OC. So, the EU had to balance these very different aspects of view and also to take account of the actions of the global AML actors. The second part of the crusade has not been easy either; the treaties of the EU/EC have not given EU/EC any competence to impose criminal law sanctions and to criminalise any acts. Even more problem has been caused the different interests and criminal justice systems and legislation of its 27 Member States and their perceptions of the sovereignty of criminal law. Also the ECJ has been active in this field by declaring judgements which have been anything but clear and thus making the crusade so complex in its nature that no one is sure what is going to happen next or what the competence of EC in criminal law matters is. And, finally, the EU has totally forgotten to establish any means of assessment using which the effectiveness its AMLS could be assessed.

1.2 Structure

The aim of this piece of a research is to critically discuss and to analyse the EU's AMLS, to describe its evolution and to analyse the effectiveness of it. This piece of research aims to recognise the structures of change in the AMLS and to analyse them critically. It also aims to give a short overview and an interpretation of the evolution of penal law and criminal policy in the EU regarding money laundering.

The second chapter of this piece of the research introduces the reader to the control policy of the European Union. The aim of the chapter is to give a short overview and an interpretation of the evolution of penal law and criminal policy in the EC/EU context. The chapter is strongly influenced by the criminological point of view. The aim of this chapter is to paint a picture how the fight against money laundering is one aspect of control policy of the EU.

The aim of the third chapter is to recognise the phenomenon of the mo-

³ S Peers, *EU Justice and Home Affairs Law* (Oxford University Press, Oxford 2006) 402-410

⁴ The word 'crusade' is used in this thesis to illustrate the difficult task the EU has had in trying to prohibit/regulate money laundering.

ney laundering. In the chapter it is considered what kind of a phenomenon the money laundering is. It is very important to draw a picture about the phenomenon in order to fully understand the countermeasures taken. However, the space does not permit any wide discussion about the phenomenon so only the major features of the money laundering are discussed. I am very unsatisfied with the Traditional -model which is used to describe money laundering process. This model is widely cited in the literature. In this piece of written work there will be put forward an argument that this model, also called Three Stage -model, is badly out-dated.

I have also wanted to bring some criminal policy views to this piece of research and thus one chapter of this thesis is devoted to arguments for and against money laundering. For my point of view this chapter brings more deepness to this work by discussing about the arguments why there in general exists any prohibitions relating to money laundering and, on the other hand, why there should not exist any. In this chapter the cost-benefit analysis, i.e. balancing the threat of money laundering and the costs of its prohibition, is seen to have an utmost importance.

In the fifth chapter the look is taken to the world-wide fight against money laundering by introducing the most important global efforts against money laundering. However, again the space does not permit any deep discussions about those instruments.

In the chapter 6 the development and the current state of the legal instruments by the EC/EU used in the fight against ML are analysed. In the chapter the double text -approach to money laundering is discussed and the legislative instruments used are carefully analysed and evaluated. There is also asked why the EU has decided to criminalise money laundering for the first place.

The chapter 7 is devoted to the critical analysis of the EU's AMLS. The SWOT -analysis, widely used in the business world, is here used to assess the EU's AMLS. In the chapter it is also concentrated on the main deficits of the AMLS, like the questions about the EC's/EU's competence to criminalise and the heavy burden of the responsabilisation/pluralisation strategy.

The effectiveness of the EU's AMLS is evaluated in the chapter 8. There is widely criticised the absence of the formal tools by the EU which would enable the assessment of the effectiveness of the EU's AMLS. There is also very short assessment of the effectiveness of the AMLS based on the information currently available. This is made in order to give at least a glimpse whether the strategy have had any effect on the money laundering phenomenon in some Member States.

1.3 Terms

1.3.1 *Dirty Money versus Clean Money*

Clean money i.e. money not earned in any criminal way can be contrasted to dirty money which is gained by using illegal means. This dirty money cannot be invested or spent on consumption without the risk of punishment because the dirty money can be used as an evidence of the initial crime. Virtually all income from criminal activities must be disguised to be of use to the criminal and money laundering is that process of disguise.⁵

1.3.2 *Pillar Structure of the European Union*

The Maastricht Treaty 1992 created the European Union as a three pillar structure. The first pillar is the EC; the second is the Common Foreign and Security Policy (CFSP); and the third pillar is the Justice and Home Affairs. The decision making, the relationship with its Member States, interaction of the principal institutions and the nature and dynamic of the law differs considerably between three pillars. The Justice and Home Affairs pillar was renamed the Police and Judicial Co-operation in Criminal Matters (PJCCM) by the Amsterdam Treaty in 1997.

1.4 Methods and Exclusions

The aim of this piece of research is to recognise the structures of change in the EU's AMLS and to analyse them critically, so the phenomenological approach is used. The criminal policy view behind the AMLS is also discussed. In this piece of research the criminological approach plays a major role, for example when the money laundering phenomenon and the rationale behind it is discussed.

Due to the lack of space the human right issues are not discussed although it is argued that in some cases the criminalisation of certain acts, also relating to money laundering, breaches human rights obligations.

1.5 Sources

The sources of this research have been mainly Anglo-American literature or journals because the phenomenon of money laundering has not attracted Finnish researchers' or lawyers' attention until very recently. However, the

⁵ P Alldridge, *Money Laundering Law* (Hart Publishing, Oxford 2003) 1

emphasis has been on the British literature and law/criminology journals although some texts of American authors like Lilley and Finnish authors like Heikinheimo and Sahavirta has been used as well. There exists no primary source in this research. I have widely used law/criminology journals as well as EC/EU documents because they contain more up-dated information than books.

2 EUROPEAN UNION AND CONTROL POLICY

'Modern societies based on increasing mobility, urbanisation, anonymity and diminishing social control provide greater leeway and increasing opportunities for OC'.⁶

2.1 The Double-Edged Sword

The Single European Act (SEA) 1986 set the creation of an 'internal market', an area without internal borders, as the target of the EU. The free movement of payments, and the establishment of a Single Payment Area, have been necessary to the achievement of free movement in goods, services and capital. The EU has also prohibited all the restrictions on the movement of capital and on payments between the Member States and between the Member States and third countries subjecting to certain rare exceptions. *The Schengen agreement*, in its turn, by removing border controls, has allowed the free movement of persons across the EU. As corollary of this criminals would have got a new, more liberal play field for their activities, a play field without internal frontiers and with single⁷ currency. So, the EU faced the double-edged sword of having open borders, in that it did aid illicit as much as licit business. In order to regulate the illicit one, the EU had to start to build a control policy of its own.

2.2 Money Laundering as a Fruit of Organised Crime

Contrast to internal market with its freedoms the EU has systematically developed its activities in the field of penal law (*spill-over effect*) and it has become a major actor in the formulation of the control policy, especially relating to OC. OC covers a range of criminal activities such as fraud, arms and drug trafficking, smuggling of radioactive and nuclear materials, trafficking in human beings, financial crime and money laundering. The political changes, like the establishment of regional trade groupings (e.g. the EU); the economic changes, like the EU and the integration of global financial markets; and technological changes, like electronic fund transfer and telecommunica-

⁶ Europol. Organised Crime Report 2005.
<http://www.europol.europa.eu/publications/Organised_Crime_Reports-in_2006_replaced_by_OCTA/EU_OrganisedCrimeReport2005.pdf> (accessed 1.11.2008)

⁷ Euro is used by more than 320 million Europeans in twenty countries.

tions, have promoted the spread of OC during the last decades.

When it comes to control policy choices, there exist different ways that can be used to tackle OC. One option is to tighten criminal law by criminalising certain acts or by reviewing of the offences. Another important thing is to ensure the international co-operation. Aside these efforts the EU has regarded the ensuring of the confiscation of the proceeds of crime as a vital part in the fight against OC. And thus it has regarded the fight against money laundering being one of its priorities in the fight against OC.

While there are well established European criminal organizations with their own specialties (mafia in Italy; money laundering in Poland; counterfeiting in Lithuania), OC is becoming even more international⁸. In its 2004 report⁹, Europol identifies a diversification of OC groups away from single specialties to multi-crime. It is seen that OC concentrates on low risk, high profit crime, such as human trafficking, smuggling and drugs. After drugs trafficking, financial crime is the favoured crime for OC groups within the EU. Polish OC groups are among the fastest growing groups in the EU, and are expanding their criminal activities all over the continent. Ethnic Albanian criminal groups pose a significant threat to the EU because of their involvement in drug trafficking and money laundering. Europol also does not afraid to warn that there is a considerable and constantly increasing number of modi operandi for the laundering of money¹⁰ although as discussed later in this thesis, there does not exist any, especially European wide, information available from which this kind of conclusion could be drawn.

Money laundering can be seen as an inherent characteristic of OC, and it can be stated that there is no OC without money laundering. Thus money laundering is regarded to be among the fifteen areas¹¹ of EU's particular interest. However, this list of 15 crimes is not a formally agreed programme but the EU has focused on these crimes in practice because of their close relationship with core EU interests, cross-border importance and political importance.

The Hague Programme 2005–2010 aims for closer co-operation between Member States in justice and security with fighting terrorism and OC through police and judicial co-operation, information sharing and border control. As

⁸ Europol. Annual Report 2006.

<<http://www.statewatch.org/news/2007/apr/europol-ann-report.pdf>> (accessed 1.11.2008)

⁹ Europol. Annual Report 2006.

<<http://www.statewatch.org/news/2007/apr/europol-ann-report.pdf>> (accessed 1.11.2008)

¹⁰ Europol. Organised Crime Report 2005.

<http://www.europol.europa.eu/publications/Organised_Crime_Reports-in_2006_replaced_by_OCTA/EU_OrganisedCrimeReport2005.pdf> (accessed 1.11.2008)

¹¹ S Peers, *EU Justice and Home Affairs Law* (Oxford University Press, Oxford 2006) 402-410

part of its control policy, the EU has set up various bodies and structures to fight against OC, like Europol (set up in 1992), Eurojust, European Judicial Network, European Forum on Organized Crime Prevention and EU Crime Prevention Network.

2.3 The Importance of the Co-operation and the Efforts of Harmonisation

The first reference to money laundering in the EU literature was made in a resolution of the European Parliament in 1986¹². Before the *Treaty on European Union* (TEU) 1992, the EU/EC did not have any competence in criminal matters although the problems caused by OC were acknowledged.

The harmonisation of the AML legislation at the Community level aims to diminish the dangers arising from illicit economic activities as well as to protect the law-abiding actors¹³, can be seen as main aims of the EU's AMLS. The EU has considered that the sole national level measures would have only a limited effect on OC.

The process of harmonisation of criminal law in the EU differs from all other relevant efforts in the field because this process takes place in the frame of a constructed supranational organisation and in the process the EU wants to protect of some 'legal goods' of the EU itself as a supranational organisation¹⁴. The activities that have attracted the interest of the EU and been subject to the harmonisation efforts have been money laundering and also for example fraud against EC's financial interests. In the EU these efforts of harmonisation of the certain parts of criminal laws of the Member States have taken place in form of different legal instruments like conventions, Joint Actions and Directives.

Although a number of international treaties has been adopted regarding the money laundering, the EU has observed that those treaties cannot fully guarantee the achievement of their objective but the EU has wanted to guarantee a greater level of harmonisation in the issue. The EU, being *sui generis* compared with other policy makers like the UN, has also unique legal instruments to be used. The reasons for this harmonisation development are

¹² P Alldridge, *Money Laundering Law* (Hart Publishing, Oxford 2003) 97

¹³ F Pappalardo 'The European Anti-Money Laundering Legislation and its Application in Italy some sociological considerations' in A Lahtinen and V Olgiati (eds), *Crime – Risk – Security* (Turku, Turun yliopiston oikeustieteellisen tiedekunnan julkaisu 1999) 68

¹⁴ M Kaiafa-Gbandi, 'The Development towards Harmonization within Criminal Law in the European Union – A Citizen's Perspective' (2001) 9/4 *European Journal of Crime, Criminal Law and Criminal Justice* 239.

simple; the time before the EU's AML measures was unstable because the Member States did not have uniform rules to deal with money laundering, i.e. the definition of money laundering, preventive methods and the nature of punishments varied between different jurisdictions. Indeed, before the Directive 91/308/EEC, only one Member State was criminalised money laundering. So, it was commonly held belief that mere unilateral measures would not be effective enough in combat against money laundering, because '*Measures adopted solely at national or even Community level, without taking account of international coordination and cooperation, would have very limited effects*'¹⁵.

The EC's competence to harmonize the criminal law of its Member States' is not only a sensitive issue but also a very complex one. It is commonly agreed that some level of harmonisation, however not unification, of criminal law is needed in order to ensure smooth international co-operation¹⁶. The growing pressure for effective protection of the financial interests of the EU and the fight against OC has forced the EU to undertake some efforts in order to harmonise certain parts of criminal laws of the Member States. The EU has considered the best way to approach money laundering problem is to increase the co-operation between the Member States and to harmonise the AML laws of the Member States by both negative and positive integration. The sphere of the measures to directly harmonise criminal law legislation is in the EU restricted to some specific fields of transnational or cross-border criminality that have been defined as common problems. *Article 31 (1) (e) TEU* states that the powers of EU '*shall include*' the adoption of measures harmonizing the definition of offences and relevant penalties in the specific areas of '*organised crime, terrorism and illicit drug trafficking*'. Tampere European Council set out a list of areas where the EU should focus on its initial efforts to harmonize substantial law, like area of money laundering. It should be also noted that the EU's third pillar powers are limited by the principle of subsidiarity, Art 2 EU and Art 5 EC.

As discussed above, the EU's AMLS forms a part of the EU's control policy, the aim of which is to tackle the OC. In order to fully understand the countermeasures taken against the money laundering is critical to understand what kind of phenomenon the money laundering is. Thus next chapter concentrates on the money laundering phenomenon by introducing the most important features of the phenomenon.

¹⁵ Recital 5 of the preamble in Dir 2005/60/EC

¹⁶ M Joutsen, *European Union and Cooperation in Criminal Matters: The Search for Balance* (Heuni paper No 25 2006) 29

3 MONEY LAUNDERING PHENOMENON – FROM THE BLACK SUITCASES TO THE LAUNDERING OF E-MONEY

“...[a]s long as there is only one jurisdiction that offers greater opacity to the ‘money trail’ than all others, it will attract the most dirty money and its existence will be enough to frustrate law enforcers”.¹⁷

The origin of the term ‘*money laundering*’ can be found in United States, where, in the days of Prohibition, the Mafia used some Chinese laundry firms and car washes as a legitimate ‘*front*’ corporations to give a clean origin to their illegal money got from trade of illegal substances like arms and prostitution.¹⁸ In almost all European languages the term ‘*money laundering*’, which was first used with a legal meaning in an American judgement in 1982¹⁹, means literally the same thing; ‘*rahanpesu*’ in Finnish, ‘*waschen*’ in German and ‘*blanchicement*’ in French.

It is not easy to give an exhaustive definition of the term ‘*money laundering*’. The term was initially limited to mean proceeds gained from drug offences but nowadays the criminal definition²⁰ of money laundering covers all the proceeds coming from variety of illegal predicate offences, mainly from the trade of illegal narcotics, arms, humans and from different kinds of frauds and corruption.²¹

The most of academics argue that money laundering can be described as a ‘*process where launderer(s) try to transform the proceeds of illegal activities into legitimate capital*’ or simply ‘*falsely claiming a legitimate source for an illegally acquired advantage*’²², the acts of falsehood may range from simple lies to highly sophisticated administrative constructions while ‘*advan-*

¹⁷ P Alldridge, *Money Laundering Law* (Hart Publishing, Oxford 2003) 20

¹⁸ S Heikinheimo, *Rahanpesu, erityisesti kriminalisoimien ja konfiskaation näkökulmasta* (Po-liisiammattikorkeakoulun tutkimuksia 6 1999) 9-10, also e.g. G Stessens, *Money Laundering. A New International Law Enforcement Model* (Cambridge University Press, Cambridge 2000) 82-83. See for further discussion: R Sahavirta, *Rahanpesu rangaistavana tekona* (Suomalainen Lakimiesyhdistys 2008) 19-21

¹⁹ US v \$4,255,625.39 (1982) 551 F Supp.314

²⁰ See R Sahavirta, *Rahanpesu rangaistavana tekona* (Suomalainen Lakimiesyhdistys 2008) for more discussion about criminal definition of money laundering and money laundering as a phenomenon.

²¹ P Lilley, *Dirty Dealing: the Untold Truth about Global Money Laundering, International Crime and Terrorism* (Kogan Page, Sterling 2006) 8

²² P van Duyne and others, *Criminal Finances and Organising Crime in Europe* (Wolf Legal Publishers, Nijmegen 2003) 69

tage' covers any material or immaterial gain.²³ One option is to see money laundering occurring where the discovery of the origin of proceeds is made impossible and forfeiture, collection and seizure are tried to make impossible or endangered.²⁴

The money laundering phenomenon has existed long time. A money launderer is traditionally seen as a suspicious man with a black top hat and a black suit standing at the counter of bank with a black suitcase full with used notes.²⁵ The oldest international mechanisms for laundering are alternative remittance systems that operate outside established regulatory systems to move value from one place to another without physical movement of money. In the past these systems were used by immigrant workers to sent money to home but nowadays these systems have developed to be channels of drug money.²⁶ But the money laundering methods have gone a long way from that. It has become a sophisticated and well-organised business of the chosen few, with technology as its driving force and all-tightening legislation as its treat. It can be argued that while growing profits in smuggling and in international frauds the need for money laundering has increased and the need for professional money launderers has grown²⁷. It should also be noted that there exists some very controversial arguments about maliciousness and disadvantages of money laundering.

Globalisation with increased deregulation, financial liberalisation and privatisation, the continuing integration of the world economy, the removal of barriers to the movement of capital, instantaneous payment systems, electronic transfers of money as well as the growth of stock markets in developing countries and diversification of financial instruments have created an enormous new play field for money launderers. The technological revolution, especially the emergence of '*cyber laundering*', has introduced new speed in the money transaction processes making money laundering even more international, a frontiers-crossing phenomenon.²⁸ Due to the development of the technology as well as the emerging AML legislation, it is argued that money laundering will also concentrate into the hands of professional launderers. It is claimed that there will be a growing demand of professional launderers,

²³ P van Duyne and others, *Criminal Finances and Organising Crime in Europe* (Wolf Legal Publishers, Nijmegen 2003) 69

²⁴ W Hetzer, 'Money Laundering and Financial Markets' (2003) 11 Eur.J.Crime Cr.L.Cr.J. 266

²⁵ P Lilley, *Dirty Dealing: the Untold Truth about Global Money Laundering, International Crime and Terrorism* (Kogan Page, Sterling 2006) xii

²⁶ P Alldridge, *Money Laundering Law* (Hart Publishing, Oxford 2003) 3

²⁷ E Savona and F Manzoni, *European Money Trails* (Harwood Academic Publishers, Amsterdam 1999) 5

²⁸ W Gilmore, *Dirty Money: The Evolution of Money Laundering Counter-Measures* (Council of Europe Press, Strasbourg 2004) 44

like accountants (so called gatekeepers²⁹) and money laundering will be made more often by custom-made than conveyer belt -style. The custom-made job, although more expensive, is usually less time-consuming and more sophisticated. When the laundering operation is made by professionals, it also gives some advances to the criminals. For example the infrastructure, like the ghost corporations, can be ready-made. A professional launderer diminishes the risk of being catch and he knows the right persons and if he is a lawyer, the criminal may have an extra protection from their confidential relationship. One problem is that money launderers are usually well educated and experienced and thus they precede the legislative measures. Also the effect of *tax havens*³⁰ is undisputed; these countries have used possibilities for anonymous investment as means to attract the investors and have not usually carefully observed the origin of the monies invested in their economy.

One of the main problems regarding the money laundering is that it is extremely difficult to gain data about the *quantum* of the proceeds laundered because some of the illegal proceeds gained are never even laundered or integrated to legal economy.³¹ The fundamental problem is how the counts should be made because there do not exist any world-wide guidelines. Thus the estimations made different ways give absolute different outcome and can skew the estimations drastically. Money laundering has thus an enormous ‘*dark figure*’. It is also contended that the politicians and law enforcers have usually bigger estimation figures about money laundering than bankers and lawyers because the latter want to whittle down proposed measures against money laundering³². The FATF estimates that money laundering industry takes from two to five percent of the world’s gross domestic product³³ exceeding \$2 trillion per year!³⁴

However, some academics hold these estimations as a mere attempt to try to convince people that the AML countermeasures are really needed, arguing that it is impossible to give any kinds of estimations about underground macroeconomics and the cross-boarder flows of cash. Van Duynе criticisers

²⁹ W Gilmore, *Dirty Money: The Evolution of Money Laundering Counter-Measures* (Council of Europe Press, Strasbourg 2004) 42-43

³⁰ The term ‘secrecy/tax haven’ does not have a clear definition but it is usually regarded to stand for jurisdiction with relatively low rates of tax, high level of banking secrecy, large financial sector, the absence of currency controls on foreign deposits and self promotion as an offshore financial sector to name a few.

³¹ G Stessens, *Money Laundering. A New International Law Enforcement Model* (Cambridge University Press, Cambridge 2000) 88

³² G Stessens, *Money Laundering. A New International Law Enforcement Model* (Cambridge University Press, Cambridge 2000) 88

³³ FATF. 40 Recommendations. <http://www.fatf-gafi.org/40Recs_en.htm> (accessed 9.9.2008)

³⁴ P Lilley, *Dirty Dealing: the Untold Truth about Global Money Laundering, International Crime and Terrorism* (Kogan Page, Sterling 2006) xiii

very harshly these kinds of estimations of money laundering volume arguing that these kinds of approaches have been accompanied more by fact creation than fact finding and merely in purpose to stimulate political action³⁵. This kind of critique can be seen to be a sort of overkill but at the same time it is easy to agree with Van Duyne who points out that if there were as much laundering as claimed, the visible effects on world economic and political order would be far more obvious³⁶. There is certainly a lack of adequate information in this field; more detailed economic analysis concerning criminal markets and organizations is definitely needed. That is the only way to build a more effective strategy against money launderers.

It is commonly agreed that money laundering is all time growing phenomenon³⁷ and that money laundering methods will become more complex – the money launderers invent new techniques and thus race against the legislative measures in well regulated countries, creating thus vicious circle of money laundering methods and legislative measures. As a response to all growing opportunities of money laundering and because of the fear of various negative effects of it, various international and national organisations have begun their AML crusade. Throughout tightening regulation especially in the financial sector has made money launderers to look for the services of the less regulated non-financial sector³⁸. In other words, money launderers are going to deeper underground. Something about the prevalence tells it that it is as easy to find institutions in the Internet which offer money laundering services³⁹ – there is certainly a different kind of supply of money laundering services nowadays than it was a couple of decades ago – the money laundering services are within reach of everyone and this has been one factor which has contributed the discussions about the need for proper AMLS at the EU level.

As already seen, the definitions of the term '*money laundering*' are vague and can differ considerably. Indeed the existing definitions have got harsh critique, they have been argued to be confused and complicated⁴⁰ as well as out-dated. They are not seen to encompass the variety of methods used to

³⁵ P van Duyne, *Money Laundering: Pavlov's Dog and Beyond*, 37 (1998) *The Howard Journal* 4 359

³⁶ P van Duyne, *Money Laundering: Pavlov's Dog and Beyond*, 37 (1998) *The Howard Journal* 4 359

³⁷ See, for example P Lilley, *Dirty Dealing: the Untold Truth about Global Money Laundering, International Crime and Terrorism* (Kogan Page, Sterling 2006)

³⁸ W Gilmore, *Dirty Money: The Evolution of Money Laundering Counter-Measures* (Council of Europe Press, Strasbourg 2004) 35-41

³⁹ Take a closer look: Privacy World <<http://www.privacyworld.com/auto/anonbank.htm>> or Offshore Manual <<http://www.offshore-manual.com/AnonymousBanking.html>>

⁴⁰ P Lilley, *Dirty Dealing: the Untold Truth about Global Money Laundering, International Crime and Terrorism* (Kogan Page, Sterling 2006) xi

launder money. The whole term is a misnomer because it fails to recognise that in the modern world the whole money laundering operation can be undertaken without any involvement of actual money.

It is essential to make clear how money laundering can happen in practice, thus in the next sub-chapters a well established but at the same time a very controversial Three Stage -model is introduced and considered.

3.1 Traditional Approach – the Three Stage -Model

Money laundering is considered being a process, not a single act.⁴¹ It is claimed that only the imagination, economic position and the contacts of the money launderers set the limits to the means how the money can be laundered. However, also the origin of the illegal money and the subsequent purpose of its use affect the method used. The money laundering process has traditionally been seen consisting of three different stages: placement, layering and integration – the model illustrating this has named as the *Three Stage -model*.

In past all of these stages were almost always clearly discernible in every money laundering operation but recently the model has got some harsh critique⁴² because, today unlike in the past, the stages may occur simultaneously, overlap or even not occur at all. As example, the proceeds gained from tax evasion do not necessary need the placement stage and thus the operation starts from layering stage⁴³. Despite the ever-growing critique to the Three Stage model, in the next chapters the model is considered and in the chapter 3.2 a new, modern approach is brought forward.

3.1.1 Placement stage – Physical Disposal of the Money

“Money laundering is seen to constitute the Achilles’ heel of organised crime, as it forces criminals to co-operate with the institutions from the legal economy⁴⁴.”

⁴¹ W Gilmore, *Dirty Money: The Evolution of Money Laundering Counter-Measures* (Council of Europe Press, Strasbourg 2004) 32

⁴² Take look to following books: P Lilley, *Dirty Dealing: the Untold Truth about Global Money Laundering, International Crime and Terrorism* (Kogan Page, Sterling 2006) and D Hopton, *Money Laundering: A Concise Guide for All Business* (Aldershot, Hants, English; Burlington, VT: Gower 2006)

⁴³ S Heikinheimo, *Rahanpesu, erityisesti kriminalisoinnin ja konfiskaation näkökulmasta* (Poliisiammattikorkeakoulun tutkimuksia 6 1999) 25

⁴⁴ G Stessens, *Money Laundering. A New International Law Enforcement Model* (Cambridge University Press, Cambridge 2000) 12-13

At the first stage, placement stage, illegal money enters into the financial system as deposits. One of the methods used in this stage is making deposits using false names and IDs which really puts pressure on the financial institutions and their ‘*know your customer*’ -principles (referred as *KYC*-principle). This is not the *only* solution available; there exist various other possibilities to carry out this stage like to use illegal money to purchase expensive goods or to invest it in real estate. The money launderers can also use their illegal cash to purchase goods that are later sold, ‘*merchandise laundering*’⁴⁵.

This stage has traditionally been by far the most vulnerable phase in the whole model because the illegal money is usually in cash and in small notes. Thus the laundering process is traditionally preferred to take place in less well regulated jurisdictions. In AML literature the geographic relocation of money is seen to be the most vulnerable part of the whole laundering process. Because large sums of cash are hard and risky to smuggle the money launderers can hire persons to convert cash into larger notes using e.g. bureaux de change, called ‘*refining*’⁴⁶. And the currency really matters, the largest Euro note is 500 and thus one million dollars in Euro weighs 2.4 kilos compared to that the same sum in largest possible dollar notes weighs about 10 kilos⁴⁷.

Although every trick in the book in the currency ‘*smuggling*’ can be used, there can be found three main ways to smuggle currencies; by shipping cash through channels used to deliver drugs, by hand-carrying by courier or criminals themselves; or changing cash into instruments like traveller’s cheques and mailing them.⁴⁸ The decreased border controls in the internal borders of EU and the common currency have made it easier to smuggle even large sums of cash from one country to other inside EU – this all increases the pressures on legislative measures of EU.

Instead transferring illegal money to other jurisdiction(s) money launderers can use method called ‘*smurfing*’ i.e. many criminals making deposits to various financial institutions just under the threshold limit of the mandatory report is a widely used method. Although the deposits of large sums of cash to financial institutions have been made more difficult for money launderers because almost all the Western countries have introduced threshold limit of the mandatory reporting or the obligation to report about suspicious transactions,

⁴⁵ P Lilley, *Dirty Dealing: the Untold Truth about Global Money Laundering, International Crime and Terrorism* (Kogan Page, Sterling 2006) 1-18

⁴⁶ W Gilmore, *Dirty Money: The Evolution of Money Laundering Counter-Measures* (Council of Europe Press, Strasbourg 2004) 33

⁴⁷ P Lilley, *Dirty Dealing: the Untold Truth about Global Money Laundering, International Crime and Terrorism* (Kogan Page, Sterling 2006) 49

⁴⁸ J Richards, *Transnational Criminal Organizations, Cybercrime, and Money Laundering: A Handbook for Law Enforcement Officers, Auditors, and Financial Investigators*. (CRC Press, Boca Raton, FL 1999)

'smurfing' can be easy if the employees of the deposit-taking institutions are corrupted. However, in Western countries, mainly confronting non-corrupt deposit-taking institutions and the increased controlling and reporting of the customers of financial institutions, the 'smurfs' have been forced to explore opportunities outside the legal financial⁴⁹.

If money launderers, especially small-scale launderers, want to avoid dealing with financial institutions they can mix legally and illegally gained profits and usually use the unlawful income for every day life expenses, to things which do not attract suspicion. Any cash-rich business like antique shops, car dealing, casinos and restaurants can be used as 'front' corporations i.e. a business type where it is accepted that cash forms the major proportion of their takings, allows the cash quite easily to be inserted into the banking system. These kinds of 'shell' corporations provide small-scale launderers opportunity for 'legitimate' income at least to certain limits although highly unrealistic revenue figures may attract suspicion⁵⁰.

Placement phase⁵¹ has been successful when all the cash has been placed into (non-)financial institutions or converted into valuable goods. The second stage in the model is layering, also called 'agitation' or 'commingling'. Layering stage can vary considerably but in this chapter only the most common methods used in this stage are considered.

3.1.2 Layering Stage – Structuring Financial Transactions to Disguise the Trail

Before the layering stage the criminal money may have been placed in the banking system but it is still in one block or can be identified as such.⁵² The *raison d'être* of this stage is to break the money up and to try to hide the paper trail by creating as much paper work as possible by carrying out various transactions subsequently or simultaneously within the same or the other financial

⁴⁹ P Lilley, *Dirty Dealing: the Untold Truth about Global Money Laundering, International Crime and Terrorism* (Kogan Page, Sterling 2006) 50

⁵⁰ W Gilmore, *Dirty Money: The Evolution of Money Laundering Counter-Measures* (Council of Europe Press, Strasbourg 2004) 38. See for further analysis, J Richards, *Transnational Criminal Organizations, Cybercrime, and Money Laundering: A Handbook for Law Enforcement Officers, Auditors, and Financial Investigators*. (CRC Press, Boca Raton, FL 1999)

⁵¹ More discussion for placement phase, see V Mitsilegas, *Money Laundering Counter-Measures in European Union: a new paradigm of security governance versus fundamental legal principles* (Kluwer Law International, The Hague 2003) Chapter 2.

⁵² P Lilley, *Dirty Dealing: the Untold Truth about Global Money Laundering, International Crime and Terrorism* (Kogan Page, Sterling 2006) 50

institution(s), all this is done only to confuse the possible investigators.⁵³ In this stage also a false paper trail can be created in order to provide false documentaries for the illegal money.⁵⁴ The key to a successful layering operation is to ensure that the layering transactions cross, physically or electronically, borders of several jurisdictions, ideally at least two jurisdictions should be included, or go through various corporations in those jurisdictions⁵⁵.

One method in this stage is to convert cash into monetary instruments; money may be invested in stocks and bonds, securities and futures markets or the proceeds can be changed into other currencies⁵⁶. To be able to do this either the money launders themselves have to be professionals or they may hire professionals like brokerage firms which are commonly used especially in the countries where identities of the beneficiaries can be concealed by holding brokerage firms as trustees⁵⁷. The 'ghost' corporations, established in *tax havens*, are typically used at this stage to facilitate the laundering.

Aside to legal market instruments, money launderers may also exploit the services of underworld, like the *underground* or *parallel banking systems*⁵⁸, like Hundi/Hawala and Chop Shop/Chitti. These underground banking systems have proved to be extremely difficult to be revealed by the authorities and the international and the regional AML measures have indeed increased the demand of those systems⁵⁹.

There are some clear characteristics which can bring to daylight that layering stage is going on, for instance the lack of investor concern over losses on investments or professional advisor charges can indicate that person owing the assets has only one motive in his transactions – to disguise the origin of his funds. Also spotting a numerous, unreasonable, transactions especially to the other jurisdiction(s) in a fairly short period of time can also

⁵³ G Stessens, *Money Laundering. A New International Law Enforcement Model* (Cambridge University Press, Cambridge 2000) 84

⁵⁴ See more: V Mitsilegas, *Money Laundering Counter-Measures in European Union: a new paradigm of security governance versus fundamental legal principles* (Kluwer Law International, The Hague 2003)

⁵⁵ J Richards, *Transnational Criminal Organizations, Cybercrime, and Money Laundering: A Handbook for Law Enforcement Officers, Auditors, and Financial Investigators*. (CRC Press, Boca Raton, FL 1999)

⁵⁶ P Lilley, *Dirty Dealing: the Untold Truth about Global Money Laundering, International Crime and Terrorism* (Kogan Page, Sterling 2006) 50-51

⁵⁷ W Gilmore, *Dirty Money: The Evolution of Money Laundering Counter-Measures* (Council of Europe Press, Strasbourg 2004) 39-40

⁵⁸ Underground banking system is also used for legal purposes. However, because of minimalist bookkeeping, it is impossible to estimate how widely these systems operate.

⁵⁹ W Gilmore, *Dirty Money: The Evolution of Money Laundering Counter-Measures* (Council of Europe Press, Strasbourg 2004) 34

reveal the laundering of illegal money⁶⁰.

3.1.3 Integration Stage – Giving Apparent Legitimacy to Criminally Derived Wealth

At the final, the integration, stage the layered funds are mixed with funds of legitimate origin. As noted, this mixing can also happen already at the placement stage. In principle the integration stage may not be needed at all or the proceeds can be returned to the criminals slowly and in small amounts⁶¹. This stage is gone through successfully when there has been created a false provenance for the source of the funds⁶².

The most simply way to give apparent legitimacy to illegal money is to use the inflated prices method⁶³. However, typical methods used in this stage are direct investments in which the funds, situated in offshore, are invested in legitimate businesses in the criminal's own country and the foreign corporation is shown as the purchaser. One variant of this method is '*loan back method*' where the criminal who has illicit funds in foreign bank account, makes an investment which he secures with a down payment of legitimate funds. To pay the balance he takes two loans, one legitimate and another from the foreign bank holding his illicit funds. He repays the loans and pays interest, making them both seem as legitimate.⁶⁴ Both of these methods are extremely sophisticated and while crossing borders of different jurisdictions, of which another is usually *tax haven*, these cash flows are really difficult to detect.

⁶⁰ P Lilley, *Dirty Dealing: the Untold Truth about Global Money Laundering, International Crime and Terrorism* (Kogan Page, Sterling 2006) 51

⁶¹ A Huhtamäki, *Rahan jäljittäminen* (Kauppakaari Oyj Lakimiesliiton kustannus, Helsinki 2000)

⁶² P Lilley, *Dirty Dealing: the Untold Truth about Global Money Laundering, International Crime and Terrorism* (Kogan Page, Sterling 2006) 50-51

⁶³ For further discuss, see V Mitsilegas, *Money Laundering Counter-Measures in European Union: a new paradigm of security governance versus fundamental legal principles* (Kluwer Law International, The Hague 2003)

⁶⁴ W Gilmore, *Dirty Money: The Evolution of Money Laundering Counter-Measures* (Council of Europe Press, Strasbourg 2004) 39-40

3.2 Modern Approach – the Chameleon Theory

“Money laundering schemes uncovered so far, are generally unsophisticated but of the very large cases involve the use of complex corporate structures and trusts as part of the laundering process”⁶⁵.

As late as a decade ago almost all the authors in this field accept the use of the Three Stage model as gospel. Even today it seems that almost every author in the AML literature tries to fit the modern implications of money laundering into the Three Stage -model and this results that the concepts have become totally blurred.

However, critics⁶⁶ of the Three Stage -model regard it too simplistic, pointing out that nowadays there need not to be any actual money involved in money laundering operation. They also argue that because the model has for many years regarded as the best explanation of the money laundering phenomenon, numerous cases have come to light where illegal proceeds have been laundered but this laundering has not been identified, simply because what happened did not match with money laundering was assumed to look like. Hopton thus suggests that a modern definition replacing the ancient model, would be “...*money laundering occurs every time any transaction takes place or relationship is formed which involves any form of property or benefit, tangible or intangible, which origins from criminal activity*”⁶⁷. This wide and flexible definition reflects the wideness the money laundering operation itself – the laundering can occur even though there is no money received or paid leaving the financial institutions in very vulnerable position.

Although the AML literature presents also some other substitute models for the Three Stage -model, like ‘*circulation*’ model, *two-phases model*, *four-sector model* and *destination/teleological model*,⁶⁸ it is totally unnecessary to try to illustrate money laundering using these models – there is not point in trying to artificially identify different stages of sometimes very simple and sometimes very unique and complex money laundering phenomenon. The only way to describe the money laundering phenomenon is to use flexible description which can cover the various forms of this ever-changing pheno-

⁶⁵ W Gilmore, *Dirty Money: The Evolution of Money Laundering Counter-Measures* (Council of Europe Press, Strasbourg 1999) 28

⁶⁶ See, for example D Hopton, *Money Laundering: A Concise Guide for All Business* (Aldershot, Hants, English; Burlington, VT: Gower 2006)

⁶⁷ D Hopton, *Money Laundering: A Concise Guide for All Business* (Aldershot, Hants, English; Burlington, VT: Gower 2006) 1-3

⁶⁸ For further discuss, see V Mitsilegas, *Money Laundering Counter-Measures in European Union: a new paradigm of security governance versus fundamental legal principles* (Kluwer Law International, The Hague 2003)

menon. In this paper Hopton's definition is seen to form *the Chameleon theory* while describing the multi-faced and ever-changing money laundering phenomenon in the best possible way it is thus suggested to be the substitute of the Three Stage -model.

It is also worth considering why money laundering should be regarded as a culpable act. In AML literature the reasons behind the AML measures are less well analysed; the literature, mainly, avoids answering to the question 'why?', and instead, it concentrates on only to describe the legislative measures taken. In next chapter the rationale behind the criminalisation of money laundering is considered and some arguments for and against criminalising money laundering are discussed.

4 RATIONALE BEHIND THE CRIMINALISATION OF MONEY LAUNDERING

*'...money laundering is the financial concomitant of the untrammelled play of market forces and their unlawful expressions. To certain extent it is a driving force, galvanizing contradictory social, political and economic systems.'*⁶⁹

The purpose of the international efforts of prohibiting money laundering is to restrict or more ideally to prevent totally criminals from making a profit from their offence. This strategy is aimed at, on the one hand, attacking the economic power of criminals in order to weaken them by preventing them benefiting from, or making use of, illicit proceeds and, on the other hand, at forestalling the nefarious effects of the criminal economy on the legal economy.

As Alexander puts it, the most basic rationale behind this criminalisation of money laundering is '*the moral wrong*' argument that '*crime should not pay*' the adage which should also work as a substantial deterrent⁷⁰. One theory behind the rationale is that when criminals are prevented from profiting their offences, they will not be able to re-invest money and thus they do not commit further offences.⁷¹ But the mere '*moral wrong*' argument is not enough to justify the criminalisation of money laundering – there needs to be other arguments as well.

4.1 Problematisation of the Money Laundering Phenomenon

It was in the 1980s when the US as the jurisdiction and the FATF as an international organisation began to see money laundering as a problem and later declared it to constitute a crime. This can be seen to indicate that the 'problem' of money laundering is not a natural given but it is a phenomenon which

⁶⁹ H Hafner cited in the article by W Hetzer, 'Money Laundering and Financial Markets' (2003) 11 Eur.J.Crime Cr.L.Cr.J. 266

⁷⁰ R.C.H. Alexander, *Insider Dealing and Money Laundering in the EU* (Aldershot, Burlington 2007) 24

⁷¹ R.C.H. Alexander, *Insider Dealing and Money Laundering in the EU* (Aldershot, Burlington 2007) 26

has been ‘problematized’ relatively recently. According to Hülse⁷² this problematisation took place step by step: firstly the FATF constructed money-laundering as a global phenomenon, then turned it into a political problem and finally regarded this problem as needing a global solution. He sees that this problematisation was the necessary first step that the FATF as an international regulator had to take when it wanted to persuade others to comply voluntarily with its rules. He argues that the rule maker has to persuade rule addressees that its rules are an effective and legitimate solution to what has earlier been constructed as a problem. This theory seems too simplistic. It is difficult to agree that one organisation, although it would have been the FATF, could have so strong an influence in so short a period. The existence of other actors like the UN should not be ignored nor should talking about the US either.

One argues that the attempts to fight against money laundering are founded on the criminal policy views originating from the US. In the US the US Treasury has considered that inadequate financial services regulation in other jurisdictions can have a direct impact on the effectiveness of financial services regulation in the US. Thus the US Treasury has the power to issue a warning to US financial institutions not to deal with financial institutions from some jurisdiction(s) in which there exist no adequate controls regarding money laundering⁷³. This pressure from the US certainly plays a great role, as it has happened also in the global ‘*war against terrorism*’. So, it seems that both the FATF and the US have both been very active in problematising the money laundering.

4.2 Money Launderers as Devil’s Advocates

Criminalisation of money laundering can be argued to have a deterrence effect on predicate crimes. Combating money laundering, and thus enabling law enforcement authorities to confiscate the proceeds of predicate criminal activities, is seen one of the most effective means of opposing OC. During the last decades there has been a clear shift in attitudes regarding the predicate crimes which have been concerned to lead money laundering. Political concerns can be seen to be behind the strategy changes in both the international and the regional AML measures; whereas in the 1980’s the major concern was seen the threat of illegal money deriving from drug trafficking, in the 1990’s there were concerns over the corrosive effect of illegal money

⁷² See, an interesting discussion about the problematisation of the money laundering in R Hülse, ‘*Creating Demand for Global Governance: The Making of a Global Money-laundering Problem*’ (2007) 21 *Global Society* 155

⁷³ R.C.H. Alexander, *Insider Dealing and Money Laundering in the EU* (Aldershot, Burlington 2007) 29

on the financial sector and now, in the 21st century's, there has been a growing concern over terrorism financing. Criminalisation of money laundering may also provide means using which evidence, found in paper trails of the laundering operation, against the top-criminals of organised crime groups can be gathered⁷⁴.

By many international and regional organisations money laundering is seen to have several negative effects on the world economy. The illegal money is feared to be used in illegal activities or to penetrate economic structures and to corrode them because illegal money is not invested effectively, emphasising the best rate of return. The money launderers do not choose jurisdictions regarding the rate of return but they choose the less well regulated jurisdiction. They also prefer conservative portfolios because they cost less than disclosure i.e. possibility of prosecution and imprisonment.⁷⁵ Thus money is moved from sound and stable economies to countries with poorer economic policies. This distorts allocation of the resources.⁷⁶ Volatility in exchange and interest rates and asset price bubbles, caused when transferring large sums of money to certain countries and especially when affecting certain single countries, are also regarded as the most frightening outcomes of laundering.⁷⁷ It is argued that small countries are particularly vulnerable to money laundering. The gains from illegal activities can provide criminal organisations with potentially huge economic power which in turn can give them leverage over small economies⁷⁸. One also argues that money laundering undermines international efforts to establish free and competitive markets and hampers the development of national economies⁷⁹.

Money laundering and illegal money can also have political influence; corruption of financial institutions and other influential institutions of legitimate economy as well as the fear of corruption of certain professionals, like lawyers, bankers and accountants is one of the most feared consequences of

⁷⁴ G Stessens, *Money Laundering. A New International Law Enforcement Model* (Cambridge University Press, Cambridge 2000) 86

⁷⁵ Further Macroeconomic effects, see P Alldridge, *Money Laundering Law* (Hart Publishing, Oxford 2003) 39

⁷⁶ G Stessens, *Money Laundering. A New International Law Enforcement Model* (Cambridge University Press, Cambridge 2000) 87

⁷⁷ Further Macroeconomic effects, see P Alldridge, *Money Laundering Law* (Hart Publishing, Oxford 2003) 39

⁷⁸ UN Model Legislation on Money Laundering and Financing on Terrorism
<<http://www.unodc.org/documents/money-laundering/2005%20UNODC%20and%20IMF%20Model%20Legislation.pdf>> (accessed 18.10.2008)

⁷⁹ UN Model Legislation on Money Laundering and Financing on Terrorism.
<<http://www.unodc.org/documents/money-laundering/2005%20UNODC%20and%20IMF%20Model%20Legislation.pdf>> (accessed 18.10.2008)

laundering.⁸⁰ Mitsilegas⁸¹ writes about ‘*myth of amoral business*’ term which he uses to refer some financial institutions’ tendency to intentionally deal with money launderers. He writes that some banks cannot only be held as victims but also as active participants in criminal businesses. Some financial institutions may be reluctant to report about suspicious transactions regarding the money launderers as they may be desirable customers because they do not demand high rates of interest and the institutions do not need to make any risky investments with launderers’ money, thus they can conform easily liquidity requirements.⁸²

Money laundering is claimed also to have effect on the socio-economic structure of countries.⁸³ The economies of many drug-producing countries are unstable and uncontrolled injection of huge amounts of money from abroad can make the inflation to rocket in some countries⁸⁴. Of course, it can be argued that some corporations while they exist to make profit, they may not care whether their products are paid using illegal funds because that does not affect their functions at all. But it is argued that money laundering can also have some drastic effects at microeconomic level. A single business can suffer severely from illegal money driven not only by complement business but also from substitutive business. In the latter case illegal goods and services are often more expensive than legal because of the monopoly position of the providers. Money laundering can also lead to dishonest competition because the corporations owned by money launderers can obtain competitive advantage because they can provide capital from illegal sources and thus they do not have to pay interest or instalments from capital money.

Money laundering is often regarded as a victimless crime, a crime without an identifiable victim. However, laundering process does not take place in vacuum – somewhere in the laundering process there is a real human suffering. Lilley claims that the people whose bank civil liberties have been removed are the direct or indirect victims⁸⁵, thus if law-abiding citizen faces false reporting as carrying out suspicious transactions, he can be seen as a victim.

⁸⁰ P Alldridge, *Money Laundering Law* (Hart Publishing, Oxford 2003) 34-35

⁸¹ V Mitsilegas, *Money Laundering Counter-Measures in European Union: a new paradigm of security governance versus fundamental legal principles* (Kluwer Law International, The Hague 2003)

⁸² P Alldridge, *Money Laundering Law* (Hart Publishing, Oxford 2003) 31-34

⁸³ M Camdessus, ‘*Money Laundering: the Importance of International Countermeasures*’ (Speech at the Plenary Meeting of the FATF on Money Laundering, 10 February 1998) <www.imf.org/external/np/speeches/1998/021098.htm> (accessed 12.4.2008)

⁸⁴ G Stessens, *Money Laundering. A New International Law Enforcement Model* (Cambridge University Press, Cambridge 2000) 5-6

⁸⁵ P Lilley, *Dirty Dealing: the Untold Truth about Global Money Laundering, International Crime and Terrorism* (Kogan Page, Sterling 2006) 60

4.3 My Beautiful Laundrette

There do exist some theories of legitimisation arguing that money laundering enables criminals to come from the shadows and to take their place in the legitimate economy. It is also suggested by some authors that it may often be beneficial to the state and to individuals to keep the origin of certain funds secret, like it happens in English law regarding the instrument of secret trust.⁸⁶

The influence of money laundering to economics is a very controversial issue because there is currently no theoretical literature available on the macroeconomic effects of money laundering⁸⁷. Mitsilegas argues that there is not enough evidence to provide that money laundering could harm regional and international economy⁸⁸. In fact there are some clear advantages in the point of view of single jurisdictions to have money laundered (not the predicate crimes taking place!) in their jurisdictions. Money laundering can be seen to mean investing money e.g. the country may get more tax revenue, job places may be created and new corporations established. For example, according to *game theory*, if some country chooses to criminalise money laundering, then it is argued that then it would be in the another country's self-interest to permit money laundering because otherwise the country allowing money laundering will receive all the profits while country criminalising the laundering bears the burdens. Thus the local measures in money laundering, like EU's, can result only in a geographical shift in the criminal activities because the money launderers' desire is to find and to take advantage of the weakest link in the global regulatory and enforcement chain, by shifting their proceeds to the countries which have weak and corruptible regulatory authorities, a restrictive bank and professional secrecy, or ineffective bank supervision. This is well illustrated by Zagaris' *the balloon* theory⁸⁹. According to the theory, there he claims that when the AML measures are tighten up in some jurisdictions, the money launderers will move to another jurisdictions, e.g. to *tax havens* where the legislation is in its infancy – as when the balloon is squeezed in some spot it will balloon to other direction. This can be seen to create a *moral purification* dilemma – the EU evicting money launders from

⁸⁶ See for further information: R.C.H. Alexander, *Insider Dealing and Money Laundering in the EU* (Aldershot, Burlington 2007) specially pages 21-23

⁸⁷ Commission of the European Communities, Second Commission Report to the European Parliament and the Council on the implementation of the Money Laundering Directive, COM final, Brussels, 1.7.1998, p. 18

⁸⁸ V Mitsilegas, *Money Laundering Counter-Measures in European Union: a new paradigm of security governance versus fundamental legal principles* (Kluwer Law International, The Hague 2003)

⁸⁹ B Zagaris, 'The emergence of an international enforcement regime on transnational corruption in the America' (1995) *Law & Pol.Int.Bus.* 53

their soil without caring that they may continue their laundering in the other countries which is maybe unable to regulate the laundering. This can lead to the exclusive club consisting of “*complying institutions*” and “*complying countries*” while the countries with a low sophistication of AML systems, mainly countries of non-European/non-American background which mostly have a weak reputation in regard to AMLS and corruption may face heavy discrimination which impacts their chances to participate international trade⁹⁰.

However, these theories of legitimisation seem to be with no foundation and only as attempts to oppose global AML efforts. The only one argument for allowing the money laundering take place that can be seen as convincing is that the criminalisation of money laundering cannot totally prevent criminals from laundering money but can drive them more underground and can make their detection even more difficult. But this reasoning is paradox because then it could be argued that criminalisation of almost every offence is unreasonable because it drives crime more underground.

Some arguments has also been cast that because of the heavy impact of the money laundering legislation to the financial institutions, i.e. the responsabilisation/pluralisation strategy including for example the reporting obligations, the burden of those institutions has increased too much and has overweighed the benefits gained from the regulation. And thus some writers suggest that the banking secrecy should be totally abolished or totally allowed and if the latter, the expenses of the financial institutions would totally disappear⁹¹. These points of view can undermine the pluralisation/responsibilisation strategy imposed by the EU in its AMLS. This is discussed later more depth in chapter 6.

One very interesting aspect is that where different AMLSs try “*to counter the use of the financial system by criminals*”, on the other hand, it is accepted that criminals use other parts of societies’ services jointly with non-criminals, for example the legal system or the health care system.⁹² Actually although in the AML literature, the effects of money laundering upon the banking system, e.g. on banking liquidity, are frequently seen as a major concern because the demands of money launderers are supposed to be more unpredictable than normal investors’ and thus the bank would need to keep more liquids to meet

⁹⁰ H Geiger and O Wuensch, ‘The fight against money laundering: An economic analysis of a cost-benefit paradox’ (2007) 10(1) J.M.L.C. 91

⁹¹ See for more discussion: P Alldrige, *Money Laundering Law* (Hart Publishing, Oxford 2003) 43 and R Sahavirta, *Rahanpesu rangaistavana tekona* (Suomalainen Lakimiesyhdistys 2008) 56

⁹² H Geiger and O Wuensch, ‘The fight against money laundering: An economic analysis of a cost-benefit paradox’ (2007) 10(1) J.M.L.C. 91

such eventualities, some different opinions are cast. For example Alldridge, Cranston and Mitsilegas impugn this adverse effect on confidence in banking arguing that there is no empirical evidence and that even the collapse of the BCCI does not support this⁹³.

It is also claimed that excessive checks to prevent money laundering can harm the competitiveness of financial institutions by increasing the direct costs of not only the illegitimate but also the legitimate market transactions and that hinders the working of '*the invisible hand*' and reduces the wealth of the nations. As a result the whole economy faces increased transaction costs for using the financial system and production costs of most services provided by the non-financial businesses and professions.⁹⁴

4.4 Pros and Cons of Money Laundering on the Scales

The creation of AML system is a complex process involving the creation or adjustment of law enforcement structures, setting up of units to receive information on suspicious transactions, the training of officials and employees of financial institutions and the introduction of internal procedures by these institutions.⁹⁵ To analyse the AMLS, a costs-benefit analysis can be used; on the other hand, weighting the costs of regulation, which include the costs of the whole criminal justice system and policing, the loss of tax revenue, cost of punishments and also less tangible costs like loss of privacy against the amount of harm money laundering causes to society⁹⁶. These costs are on the other side of the scales and on the other are the benefits gained when AMLS is implemented. Actually one of the major concerns lately has been that AMLSs with strict KYC/CDD –policies may impose threat to the privacy of the individuals – it can be even argued that criminals have won if the law-abiding citizens face in their every-day life precautions which make their life more complex e.g. filling piles of forms when opening bank account.

Sahavirta⁹⁷ among other authors very successfully weighs the arguments for and against money laundering by concluding that there would be more costs if predicate crimes and money laundering would be allowed to take

⁹³ P Alldridge, *Money Laundering Law* (Hart Publishing, Oxford 2003) 38

⁹⁴ H Geiger and O Wuensch, 'The fight against money laundering: An economic analysis of a cost-benefit paradox' (2007) 10(1) J.M.L.C. 91

⁹⁵ P Cullen 'The European Community Directive' (1993) 1(2) Hume Papers on Public Policy 189

⁹⁶ The rational choice theory. More discuss: G Becker 'Crime and Punishment: An Economic Approach' (1968) J.Pol.Econ. 76

⁹⁷ R Sahavirta, *Rahanpesu rangaistavana tekona* (Suomalainen Lakimiesyhdistys 2008) 57

place than the costs of their regulation. It would be interesting to see how she has evaluated the costs of the prevention as well as what she sees to be a suitable level of prevention.

This analysis shows that there can be certain benefits to allow money laundering to take place. This can explain why some countries can be very reluctant to begin their AML battle. However, many of the arguments discussed above can be seen as mere hypotheses – there exist no exact and absolute information about the impacts of money laundering, only presumptions. The fact is that the effects of money laundering still remains under-researched and the rationales behind the prohibiting/regulating money laundering manifold and incomplete and also at least partly unconvinced. More information about the impacts of money laundering is needed in order to assure people that money laundering is a real crime, with weak arguments this is not possible.

It can be noted that money is a powerful tool, and millions of it in wrong hands can result devastating consequences in world economy and politics. However, how drastic countermeasures should be taken to avoid this? Which kinds of measurements are proportionate and which overkill? The general hypothesis is the more effective AML regulation is the more expensive it is to launder money and the less likely money laundering takes place⁹⁸.

⁹⁸ J Harvey, *'An evaluation of money laundering policies'* (2005) 8(4) J.M.L.C. 340

5 GLOBAL WAR AGAINST MONEY LAUNDERING

“The global financial system provides many more opportunities [for money launderers] than law enforcement can ever hope to forestall or block. Consequently, law enforcement is playing a game to catch-up that it is almost certainly destined to lose.”⁹⁹

Last decades have seen many international and regional conventions to be issued whose aims have been to reduce international, national and regional vulnerabilities regarding OC. More and more governments and international and regional organisations in the 21st century consider the fight against money laundering as one of their top priorities and thus many considerable efforts have been made in recent years at the national, regional and international level. But why has money laundering, which is now one of the *major forci* of central policing agencies world-wide, attracted so little attention until relatively recently? Why have Governments and especially the EU woken up this problem so late?

The purpose of this chapter is to introduce the most influential global actors and their tools used in the global fight against money laundering. The reason for this is that all EU’s AML measurements have widely been built on them. It will be also claimed later in this thesis that the EU itself has been less innovative in its AMLS and only copy-catted those measures taken by global aml actors.

5.1 The Great Amount of the Global Anti-Money Laundering Actors – Does the Amount Substitute the Quality?

The first international AML measurements, targeting the laundering of proceeds deriving from drug trafficking, emerged in the 1980’s. However, these measures have during the years become more rigorous by reflecting more the sophistication of money laundering techniques. These international conventions have been largely ‘*hard*’ law¹⁰⁰ obligations, although alongside them also ‘*soft*’ law¹⁰¹ instruments are being used. In fact ‘*soft*’ laws have had

⁹⁹ P Williams, ‘*Money Laundering*’ (1997) 5 SAJIA 71

¹⁰⁰ ‘Hard’ laws need to be ratified by state party before it comes to effect.

¹⁰¹ ‘Soft laws’ are non-binding e.g. recommendations.

an impressive influence in the world-wide fight against money laundering, partly due to their nature, the absence of a formal international legislator. Specially regarding the financial sector they have been priceless.

The international measures taken to root out money laundering are branded by different policy implications in different decades and by different organisations – reflecting the ever-changing nature of the money laundering phenomenon. The 1980's can be seen the decade when the pioneering steps in the international AML crusade was taken and the foundation laid for the today's AMLs.

'International war against drugs' led to adoption the Council of Europe's *Recommendation No. R (80) 10, Measures against the transfer and safeguarding of the funds of criminal origin*. The United Nations (UN) also began its global crusade against money laundering by publishing *Convention on Illicit Drugs and Psychotropic Substances 1988 (Vienna Convention)*. Vienna Convention was the first international convention which criminalised money laundering. The origins of the Convention can be traced back to two earlier anti-drug conventions: *the 1961 Convention on Narcotic Drugs* and *the 1971 Convention on Psychotropic Substances*. The Vienna Convention required states to consider money laundering as a criminal offence in their national legislation and to empower the courts to order bank, financial or commercial records to be made available to the enforcement agencies, notwithstanding any bank secrecy laws. *Article 3* of the Convention provides a comprehensive definition of money laundering and it has been the basis of almost all subsequent legislation like the EU's AMLS. But the Convention is not mandatory in its nature – there is no obligation for states to prohibit money laundering. This recommendation –style approach has continued in the global AML regime.

The late 1980's also aroused the desire to protect the financial sector from money launderers and to maintain public confidence to financial institutions. In 1988 *the Basle Committee on Banking Regulations and Supervisory Practices* issued *the Basle Statement of Principles* aimed to prevent use of the banking sector for money laundering proposes, taking account also the offshore banks. The Statement played a pioneer role; it contained a number of principles regarding good banking practices, like the customer identification, staff training and ethical standards. But although the Statement was a non-binding legal document and its implementation depended on national legislative, it provided a framework of rules in an area where formal legislation was still lacking.

The 1980's culmination of the AML measures can be seen to have taken

place in 1989 when G7 countries created the FATF¹⁰² (*the Financial Action Task Force*). All Member States are now members of the FATF, the leading world AML body. The sole purpose of the FATF is to combat global financial crime. With its 40+9 Recommendations, the first issued in 1990 and several updated subsequently, in order to reflect changes in money laundering techniques and trends, the FATF has been model for many subsequent legislative measurements. The 2003 Recommendations are considerably more detailed than the previous ones, in particular with regard to customer identification and due diligence requirements, suspicious transactions reporting requirements and seizing and freezing mechanisms. The 40+9 Recommendations, covering e.g. provisional measures and confiscation, financial institution secrecy law, CDD, RSTs, record-keeping and terrorist financing, are designed to be guidelines only, recognising that each member state has its own political and legal systems. According to the first FATF Recommendation, each country should ratify and implement fully the Vienna Convention.

The FATF, based on mutual evaluations and peer pressure, has become the world's leading body in combat of money laundering. Its main purpose is to establish and promote more additional preventive methods for the fight against money laundering and especially to include the adaptation of the legal and regulatory systems as to enhance multilateral judicial assistance¹⁰³. The list of the Non-Co-operative Countries¹⁰⁴ and Territories tries to compromise the certain countries disobeying the FATF regulations and thus aiming to pressure these countries to criminalise money laundering and thus root out *tax havens*. This '*black list*' is the first effort in the global AML regime in order to punish non-co-operative countries in some way. The FATF has been very successful with its 'black list' being able to establish an effective means of deterrence without criminal law sanctions. It has been also through FATF initiative that member countries have created Financial Intelligence Units (FIUs).

In the early 1990's, the international co-operation in the fight against organised crime was seen as utmost important. At the regional level, as a result of this, the Council of Europe's *Convention on Laundering, Search, Seizure and Confiscation of the Proceed from Crime (Strasbourg Convention)* was

¹⁰² Committee of Experts on the Evaluation of Anti-Money Laundering Measures and the Financing of Terrorism (MONEYVAL) was established in 1997. This evaluation and peer pressure mechanism reviews the anti-money laundering measures and measures to counter the financing of terrorism in Council of Europe member States (and Council of Europe applicants which apply to join the terms of reference) which are not members of the FATF. Moneyval. <<http://www.coe.int/t/dghl/monitoring/moneyval/>> (accessed 28.10.2008)

¹⁰³ FATF webpage. <http://www.fatf-gafi.org/pages/0,2966,en_32250379_32236836_1_1_1_1_1,00.html> (accessed 28.6.2008)

¹⁰⁴ P Aldridge, *Money Laundering Law* (Hart Publishing, Oxford 2003) 89

entered into force in 1993. Its aim was to facilitate international co-operation and mutual assistance in investigating crime and to track down, to seize and to confiscate the proceeds of crime.¹⁰⁵

It was also 1990's when the BCCI crisis drew the attention to the need to regulate financial institutes even more and to the growing need to control money laundering more at international level.¹⁰⁶ *The Basel Committee on Banking Supervision* in 1997 developed a set of *Core Principles for Effective Banking Supervision* which provided a comprehensive blueprint for an effective supervisory system in order to promote sound supervisory standards worldwide¹⁰⁷.

The new millennium has changed the emphasis of the AMLs again; now the countermeasures against terrorism are seen having the utmost importance. In 2001, the development of standards in the fight against terrorist financing was added to the mission of the FATF. In May 2005 it issued *Detecting and Preventing the Cross-Boarder Transportation of Cash by Terrorists and Other Criminals*.¹⁰⁸ Also the Council of Europe issued *Convention on laundering, search, seizure and confiscation of the proceeds from crime and on the financing of terrorism* in 2005¹⁰⁹.

One of the main actors in this field of the global fight against money laundering has been the UN. Aside the watershed Vienna Convention, it has also developed the *Global Programme against Money Laundering* (GPML) which has many different objectives like to assist in the achievement that all States have legislation that give effect to universal legal instruments related to AML and to enhance international and regional co-operation on combating the financing of terrorism.¹¹⁰ GPML has also developed in collaboration with UNODC's Legal Advisory Section and International Monetary Fund (IMF) model laws to assist countries in setting up their AML legislation in

¹⁰⁵ The European Community is not a party to the 1990 Convention although all its 25 Member States are. J Handoll, *Capital, Payments and Money Laundering in the European Union* (Dublin, William Fry 2006) 115

¹⁰⁶ P Alldridge, *Money Laundering Law* (Hart Publishing, Oxford 2003) 38

¹⁰⁷ History of the Basel Committee. <<http://www.bis.org/bcbsh/history.htm>> (accessed 28.6.2008)

¹⁰⁸ The FATF, '*Detecting and Preventing the Cross-Border Transportations of Cash by Terrorists and Other Criminals*' (Recommendations published by the FATF in 12 Feb 2005) <<http://www.fatf-gafi.org/dataoecd/50/63/34424128.pdf>> (accessed 9.9.2008)

¹⁰⁹ Council of Europe, '*Council of Europe Convention on Laundering, Search, Seizure and Confiscation of the Proceeds from Crime and on the Financing of Terrorism*' Doc CETS No.: 198 <<http://conventions.coe.int/Treaty/Commun/QueVoulezVous.asp?NT=198&CM=1&CL=ENG>> (accessed 16.7.2008)

¹¹⁰ UN. Objectives of the Global Programme against Anti-Money Laundering. <<http://www.unodc.org/unodc/en/money-laundering/programme-objectives.html>> (accessed 8.10.2008)

full compliance with the international legal instruments, and in particular the 40+9 Recommendations, *the 1988 United Nations Convention against Illicit Traffic in Narcotic Drugs and Psychotropic Substances* and *the 2000 United Nations Convention against Transnational Organized Crime*. 'Model law on money laundering and the financing of terrorism' is the outcome of a joint effort of the United Nations Office on Drugs and Crime (UNODC) and the International Monetary Fund (IMF). It contains a comprehensive set of legal measures that a domestic law should include in order to prevent, detect and sanction effectively money laundering and the financing of terrorism and to enable international cooperation against these crimes. It is based, to a large extent, on the relevant international instruments concerning money laundering and the financing of terrorism and incorporates the FATF 40+9 Recommendations.

Furthermore, in the 21st century *the UN Convention against Transnational Organized Crime* and *the UN Convention against Corruption* have come into force by widening the scope of the money laundering offence by stating that the proceeds of all serious crimes should be covered and also urge the establishment of FIUs¹¹¹. Both Conventions call for States to create a comprehensive domestic supervisory and regulatory regime for banks and non-financial institutions, including natural and legal persons, as well as any entities particularly susceptible to be involved in a money laundering scheme.

The Wolfsberg Anti-Money Laundering Principles, established 2000, in turn, focus on the drafting AML guidelines for banks. They have concentrated on the development of a due diligence model for financial institutions and also established different sets of guidance, for example *Guidance on a Risk Based Approach for Managing Money Laundering Risks*, *AML Guidance for Mutual Funds and Other Pooled Investment Vehicles* and also guidelines relating to Beneficial Ownership, Politically Exposed Persons (PEPs) and Intermediaries.¹¹²

Interpol has also a police division which has responsibility for money laundering and related issues through its FOPAC (*Fonds Provenant des Activités Criminelles*) group established in 1983. For that purpose the FORPAC

¹¹¹ The Egmont Group, founded 1995, consists of 108 financial intelligence units (FIUs) from across the world. Financial intelligence units are responsible for following the money trail, to counter money laundering and terrorism financing. Egmont Group.

<http://www.egmontgroup.org/PRESS_RELEASE_version_27_MAY_2008_G.pdf> (accessed 25.10.2008)

¹¹² Wolfsberg Principles. <<http://www.wolfsberg-principles.com/>> (accessed 29.10.2008)

Bulletin and FORPAC's Financial Assets Encyclopaedia are used.¹¹³ Also the World Customs Organisation (WCO), consisting over 160 Member countries, has taken a part in the global AML fight. It has for example adopted a recommendation on the need to develop and strengthen the role of customs administrations in tackling money laundering and recovering the proceeds of crime¹¹⁴.

As seen in this chapter, before the EU started to establish its AMLS in the beginning of the 1990's there was already some international conventions in the field. And this global field of AML efforts has developed radically during the last decade. So, the EU have had buffet of different strategy choices from which the most suitable ones has been picked for its AMLS.

¹¹³ Interpol. Funds Derived From Criminal Activities. <<http://www.interpol.int/public/FinancialCrime/MoneyLaundering/default.asp>> (accessed 26.10.2008)

¹¹⁴ World Customs Organisation. <http://www.wcoomd.org/home_about_us.htm> (accessed 30.10.2008)

6 EUROPEAN UNION'S ANTI-MONEY LAUNDERING ARCHITECTURE

“The fight against money laundering and terrorist financing is a political priority for the EU... The EU is setting an example to be followed and matched.”¹¹⁵

When the EU started to consider the establishment of its own AMLS, it saw unilateral national measures as ineffective in fighting against OC and against money laundering. The most important legal instruments used in the fight against money laundering in the EU are three AML Directives. Those three Directives are however a part of a larger jigsaw puzzle, the other pieces being FWDs, Joint Actions and regulations.

This chapter begins by discussing why the EU in the first place has wanted to prohibit money laundering. Then the look is taken into the evolution of the EU's AMLS. Aside introducing the double-text -approach the contents of the legal tools, used to regulate money laundering, are also carefully analysed.

6.1 Rationale behind the Anti-Money Laundering Strategy

“...[F]ar from being restrictive in nature and/or an obstacle to liberalisation, a successful effort against money laundering is in fact an essential pre-condition for enhancing international trade and commerce, financial market liberalisation and the free movement of capital under optimal conditions”.¹¹⁶

Rationales behind the AMLS adopted by the EU are various. According the Article 29 TEU *‘the Union’s objective shall be to provide citizens with a high level of safety within an area of freedom, security and justice by developing common action among the Member States in the fields of police and judicial*

¹¹⁵ McCreedy C, ‘Approval of new directive will boost fight against money laundering and terrorist financing’ (Press release 26.05.2005, reference IP/05/616) <<http://europa.eu.int/rapid/pressReleasesAction.do?reference=IP/05/616&format=HTML&aged=0&language=EN&guiLanguage=en>> (accessed 14.6.2008)

¹¹⁶ Opinion of the Economic and Social Committee on the ‘Proposal for a European Parliament and Council Directive amending Council Directive 91/308/EEC of 10 June 1991 on prevention of the use of the financial system for the purpose of money laundering’ OJ C 075, 15.3.2000

cooperation in criminal matters'. That objective shall be achieved by 'approximation, where necessary, of rules on criminal matters in the Member States, in accordance with the provisions of Article 31(e)'. The EU has decided that although in some areas the mutual recognition is regarded the best way to approach, prevention and control of money laundering is one of the key areas in which the harmonisation of laws is used.

All serious criminal behaviour like money laundering should be approached in an equally efficient way thought the EU. If serious criminal conduct receives an equivalent response and procedural guarantees are comparable throughout the Union, there are better possibilities of improving coordination of prosecution.¹¹⁷ This efficiency and subsidiarity arguments have been also put forward in the *Directive 2005/60/EC on the prevention of the use of the financial system for the purpose of money laundering and terrorist financing*. It states in its preamble that 'In order to avoid Member States' adopting measures to protect their financial systems which could be inconsistent with the functioning of the internal market and with the prescriptions of the rule of law and Community public policy, Community action in this area is necessary'¹¹⁸.

In the point of view of the theory of criminalisation the rationale behind why the EU at all has interfered with the criminalisation of money laundering is that the EU has wanted to protect some 'legal goods' (*Rechtsgut*)¹¹⁹ which it has considered to be important for it. The EU has seen it important to protect its financial interests and has thus seen OC and money laundering imposing a great treat to them. Because the task to protect these legal goods is the task of the Member States, the EU had to demand the Member States to criminalise the act of money laundering¹²⁰. Among reasons for legislative actions one often refers to need to recognise certain interests *truly European*¹²¹.

*The First European Directive on Prevention of the Use of the Financial System for the Purpose of Money Laundering*¹²² was accompanied by a length preamble that provided a justification for criminalising the money launder-

¹¹⁷ Action Plan of the Council and the Commission on how best to implement the provisions of the Treaty of Amsterdam on an area of freedom, security and justice - Text adopted by the Justice and Home Affairs Council of 3 December 1998 para 18

¹¹⁸ The preamble in Directive 2005/60/EC of the European Parliament and of the Council of 26 October 2005 on the prevention of the use of the financial system for the purpose of money laundering and terrorist financing. *OJ L 309, 25.11.2005*

¹¹⁹ S Melander, *Kriminalisointiteoria – rangaistavaksi säätämisen oikeudelliset rajoitukset* (Suomalainen Lakimiesyhdistys, Helsinki 2008) 378

¹²⁰ The principle of loyalty, Article 10 TEU.

¹²¹ K Nuotio, 'On the significance of Criminal Justice for A Europe 'United in Diversity'' in K Nuotio, *Europe in Search 'Meaning and Purpose'* (Forum Iuris, Helsinki 2004) 180

¹²² Directive 91/308/EEC of 10 June 1991 on prevention of the use of the financial system for the purpose of money laundering. *OJ L 166, 28.6.1991*

ing. According to it, “*the soundness and stability of the institution concerned and confidence in the financial system as a whole could be seriously jeopardized, thereby losing the trust of the public*” if money laundering would not be criminalized. Money laundering was also seen to constitute a particular threat to Member States’ societies and being a very important component of organized crime,¹²³ there was ‘*to set a high standard in protecting the financial sector and other vulnerable activities from the harmful effects of the proceeds of crime*’¹²⁴. Also fear of the political influence of illegal monies especially from drug trade and thus e.g. corruption of financial institutions and other influential institutions of legitimate economy can be seen as driving force behind the EU’s AMLS. Also the fear of terrorism in the 21st century has been a motor for ever-sophisticating regulation. It is worth to notice that until the mid-1980s the political and public opinion perceived that almost none of the European countries were affected by organised crime¹²⁵.

The long tradition of legislative measures against money laundering in the US can be seen to have created pressure for money launderers to look for new opportunities outside the US. The EU area without internal borders can be seen to be one possible choice for them. This is also taken account in the Directive 2005/60/EC which states that ‘*In order to facilitate their criminal activities, money launderers and terrorist financiers could try to take advantage of the freedom of capital movements and the freedom to supply financial services which the integrated financial area entails, if certain coordinating measures are not adopted at Community level*’¹²⁶. However, the situation of the EU is two fold; firstly in the EU area there should be guaranteed the four freedoms, indeed Article 56 of the EC Treaty prohibits a general ban of even limitation on the import/export of capital in the area although Article 60 EC provides some room for measures limiting the freedom of capital on grounds of foreign policy or security. So the EU has to be able to balance between this two aspects – the scale cannot be too heavy on the other side.

European Commission has seen that organised financial crime undermines legitimate economic actors and strengthens the shadow economy, thus diminishing economic growth and public resources. It sees the fight against money laundering one of the top political priorities of the EU. It also criticizes the common practice to see financial crime often as a “victimless” crime

¹²³ The preamble in Directive 91/308/EC

¹²⁴ Recital 1 in the preamble Directive 2001/97/EC of the European Parliament and of the Council of 4 December 2001 amending Council Directive 91/308/EEC on prevention of the use of the financial system for the purpose of money laundering. *OJL 344*, 28.12.2001

¹²⁵ Paoli L and Fijnaut C, ‘*Organised Crime and Its Control Policies*’ (2006) 14/3 *European Journal of Crime, Criminal Law and Criminal Justice* 302

¹²⁶ The preamble in Directive 2005/60/EC

by arguing that organised financial crime may not always impact directly on individuals. However, the reality is that its broader social impact is considerable in terms of lost revenues, loss of reputation and the fall in public standards¹²⁷.

The international AML measures issued by various international organisations have had a great effect on the EU's AMLS. Alexander¹²⁸ agrees with Hülse¹²⁹ while writing about the political reality of international pressure regarding the criminalising the money laundering. He sees the pressure of prohibiting money laundering in the EU stemming from two directions: from one powerful jurisdiction i.e. from the US and from the global AML actors. Especially the UN and the FATF have had a major effect on the content of the EU's AMLS.

The US has been forerunner in world's AMLSs and thus money launderers could have felt pressure to move to other jurisdictions, and the EU with its common internal market and stable economy could have been a good resort because the desire of the groups is to minimize law enforcement risks and to maximize their opportunities that could have driven them to the EU area if it had failed in its AMLS. Others can argue that pressure from the US forced the EU to show the world that they want to act in a united manner. The EU also wanted to avoid the risk of illegal enterprise that could incur when organised groups (e.g. mafia) exercise criminal activities in several countries¹³⁰. Also the fear of the impacts of the unlawful money transactions to its monetary policy and macroeconomics, although the effect of money laundering on the latter is controversial, has been one of the driving forces¹³¹.

On the other hand, one can argue that the EU may have had some clear advantages to allow money laundering on its soil, like to get more tax revenue, more investments, new job places and flourishing financial institutions and to save huge sums of money because costs of regulation as well as criminal justice systems.

It can be clearly seen that the US and the FATF origin propaganda relating to the harmfulness of money laundering has been adopted in the EU

¹²⁷ Communication from the Commission to the Council and the European Parliament on the prevention of and fight against organised crime in the financial sector [COM(2004) 262 final - Not published in the Official Journal]

¹²⁸ R.C.H. Alexander, *Insider Dealing and Money Laundering in the EU* (Aldershot, Burlington 2007) 29

¹²⁹ R Hülse, 'Creating Demand for Global Governance: The Making of a Global Money-laundering Problem' (2007) 21 *Global Society* 155

¹³⁰ F Pappalardo 'The European Anti-Money Laundering Legislation and its Application in Italy some sociological considerations' in A Lahtinen and V Olgiati (eds), *Crime – Risk – Security* (Turku, Turun yliopiston oikeustieteellisen tiedekunnan julkaisu 1999) 68

¹³¹ W Hetzer, 'Money Laundering and Financial Markets' (2003) 11 *Eur.J.Crime Cr.L.Cr.J.* 266

institutions without any doubts. The rationales of the EU to regulate money laundering are strongly related to the to the argued adverse effects of money laundering and also the possible positive effects which one country could get if allowing money laundering to take place in its jurisdiction.

However, in reality it is impossible totally to root out the money laundering because that would need so huge sums of money. And thus this idea is totally unreasonable. Instead, criminological theories underline that, because of the scarce resources in the society, each chooses the crime level it can tolerate¹³². According to this theory the AMLS should bring the reigned level of money laundering in the EU as optimal because the net expenses of the laundering should then be the lowest possible¹³³. It seems that because of the EU has decided to demand criminalisation of money laundering it has also taken account the social cost evaluation which requires the rational evaluation of social costs and benefits of criminalisation and does not allow criminalisation if it produces more harm than benefit to certain society¹³⁴. However, the decision-making may not be as rational as this theory may emphasize, and furthermore, it is impossible to even calculate the impact of money laundering to economy.

In the following chapters the evolution of the EU's AMLS is discussed and the main legislative tools used in that strategy are evaluated. The aim of the chapter is to analyse the contents of the most important legislative tools used in the EU's AMLS.

6.2 Evolution of the EU's Anti-Money Laundering Strategy

Already in the 1980's the EC regarded money laundering demanding some urgent measurements, mainly to combat the illegal money deriving from drug trafficking.¹³⁵ However, before the *Treaty on European Union* (TEU) 1992 the EC did not have any competence in criminal matters although the problems caused by transnational crime were acknowledged. Prior to its entry into force the discussions regarding the transnational crime took place primarily

¹³² D Garland, 'The Limits of the Sovereign State' (1996) 36 *Brit.J.Criminol.* 445

¹³³ More discuss: G Becker 'Crime and Punishment: An Economic Approach' (1968) 76 *J.Pol. Econ.* 169

¹³⁴ S Melander, *Kriminalisointiteoria – rangaistavaksi säätämisen oikeudelliset rajoitukset* (Suomalainen Lakimiesyhdistys, Helsinki 2008) 502

¹³⁵ K Magliveras, 'The European Community's Combat Against Money Laundering: Analysis and Evaluation' (1998) 5 *Journal of International & Comparative Law* 91

within the framework of European political co-operation¹³⁶. The conventions adopted by the Council of Europe were no longer regarded as sufficient and effective enough to keep up in the pace of the integration of the European Communities. And while the European Communities integration continued in 1990's; the TEU created the Single Market and laid down the framework for *European Monetary Union*, introducing *Euro*, the money laundering problem did not escaped the attention; not only was the first Directive relating to AML adopted in 1991 but also TEU established a co-operation in the fields of justice and home affairs, so called '*third pillar*'. *Articles 29-31* of TEU declared preventing and combating terrorism as well as unlawful drug trafficking and other serious forms of international crime as matters of common interest in the EU. This third pillar did not create new supranational law and did not thus give any explicit basis for approximation of criminal law but a formal framework which enabled the EU to put on pressure on Member States in order to be able to improve mutual assistance and co-operation in criminal cases. However, it was made clear that from there onwards judicial co-operation in criminal cases was in a common interest of all Member States and also some new legal instruments like Joint Actions, joint positions and European conventions were introduced. Because of political pressure for action and especially concerns relating to drug trafficking, the EU started some efforts to harmonise substantial criminal law by adopting a series of third pillar measures in the years following TEU.

During the Maastricht era the EU introduced Joint Actions like *Joint Action of 17 December 1996 concerning the approximation of the laws and practices of the Member States of the European Union to combat drug addiction and to prevent and combat illegal drug trafficking*¹³⁷ and *Joint Action of 3 December 1998 on money laundering, the identification, tracing, freezing, seizing and confiscation of instrumentalities and the proceeds from crime*¹³⁸ (amended by a FWD 2001 OJ L 182/1). The effect of these Actions was however limited because they do not require Member States to amend their national law but only to present proposals to their national parliaments.

In 1997 the EU issued a Plan of Action in order to fight against OC. That changed the pace of evolution of the EU's AMLS. This included the adoption of decisions related to the criminalisation of money laundering like

¹³⁶ W Gilmore, *Dirty Money: The Evolution of Money Laundering Counter-Measures* (Council of Europe Press, Strasbourg 2004) 193

¹³⁷ Joint Action 96/750/JHA of 17 December 1996 adopted by the Council concerning the approximation of the laws and practices of the Member States of the European Union to combat drug addiction and to prevent and combat illegal drug trafficking. OJ L 342, 31.12.1996

¹³⁸ Joint Action 98/699/JHA of 3 December 1998 adopted by the Council on money laundering, the identification, tracing, freezing, seizing and confiscation of instrumentalities and the proceeds from crime. OJ L 333, 9.12.1998

Joint Actions. Two years later in 1999 in the European Council meeting in Tampere money laundering was condemned to be rooted out because it was seen to be ‘*at the very heart of organised crime*’. The main step was that also the approximations of criminal law as well as uniform scope of predicate offences for money laundering to all Member States were called for.¹³⁹ Tampere programme also refers to ‘*the necessary approximation of legislation*’¹⁴⁰. But what was meant by ‘necessary’ was unclear. The period allotted for the Plan of Action ended by the 2000 and follow-up plan ‘*The Prevention and Control of Organised Crime: A European Union Strategy for the beginning of the new Millenium*’, with specific focus on e.g. money laundering, was adopted in 2000. The success of the Tampere programme has been criticised; the programme has been seen to have provided insufficient direction and as a proof for this is seen the inability of the Commission or the Member States to submit any legislative proposals based on a well thought-out enforcement and criminal law policy¹⁴¹. Ladenburger¹⁴² argues that the high political ambition expressed by the European Council for example in Tampere meeting and in Hague Programme have been fatally undermined because of the shortcomings in the institutional framework set up under the current third pillar.

The revision of the EU Treaty by *the Treaty of Amsterdam* (ToA) and *the Treaty of Nice* brought some new legal instruments. The objective of the third pillar stated in the ToA, was to create a security community, an area of ‘*freedom, security and justice*’¹⁴³. Besides by introducing new legislative tool Framework Decision, the ToA also emphasis on the importance of the progressive harmonisation of important criminal law provisions in the Member States. TOA declares that it shall be achieved by minimum rules relating to the constituent elements of criminal acts and to penalties in the fields of OC, terrorism and illicit drug trafficking¹⁴⁴.

The fight against drugs and the protection of financial institutes turned in the 21st century to fight against terrorism and also the co-operation between countries became more important. Two important FWDs were issued: *a Council Framework Decision of 24 February 2005 on Confiscation of Crime-*

¹³⁹ European Council, ‘Tampere Presidency Conclusions’ (15 and 16 October 1999) Doc SN 200/99. Paragraphs 51, 55, 57

¹⁴⁰ European Council, ‘Tampere Presidency Conclusions’ (15 and 16 October 1999) Doc SN 200/99. Paragraph 37

¹⁴¹ A.E. Vervaele, *The European Community and Harmonization of the Criminal Law Enforcement of Community Policy*, Eucri 3-4 (2006) 88

¹⁴² C Ladenburger, ‘*Police and Criminal Law in the Treaty of Lisbon*’ (2008) 4 *European Constitutional Law Review* 20

¹⁴³ Article 40 of the Treaty of Amsterdam 1999

¹⁴⁴ Art 31 TEU

*Related Proceeds, Instrumentalities and Property*¹⁴⁵ and a Council Framework Decision of 22 July 2003, on the execution in the European Union of orders freezing property or evidence¹⁴⁶. Also a Convention of 29 May 2000 on Mutual Assistance in Criminal Matters between the Member States¹⁴⁷, which provides a framework for EU police and legal cooperation and procedures to be followed, was issued.

Europol was also taken along to the fight against money laundering by the Council Act of November 2000 amending the terms of the Europol Convention. This extended the competence of Europol to money laundering in general, not just drugs-related money laundering¹⁴⁸.

6.3 Legal Instruments Used in the Fight against Money Laundering – the Double Text Approach

The EU has used different legislative instruments, like Joint Actions, FWDs and Directives in the fight against money laundering. The picture below shows so called double-text approach which the EU has taken in its AMLS. Similar approach is also found in the strategy of *protecting of Euro against counterfeiting* and in the EU's *anti-terrorism* strategy.

¹⁴⁵ Council Framework Decision 2005/212/JHA of 24 February 2005 on Confiscation of Crime-Related Proceeds, Instrumentalities and Property. OJ L 68, 15.3.2005

¹⁴⁶ Council Framework Decision 2003/577/JHA of 22 July 2003, on the execution in the European Union of orders freezing property or evidence. OJ L 196, 2.8.2003

¹⁴⁷ It should be noted that for money laundering there is a relevant convention of the Council of Europe but this double regulation has a practical meaning because of different legal orders i.e. Council of Europe and EU.

¹⁴⁸ Convention on the establishment of a European Police Office. OJ C 316, 27.11.1995

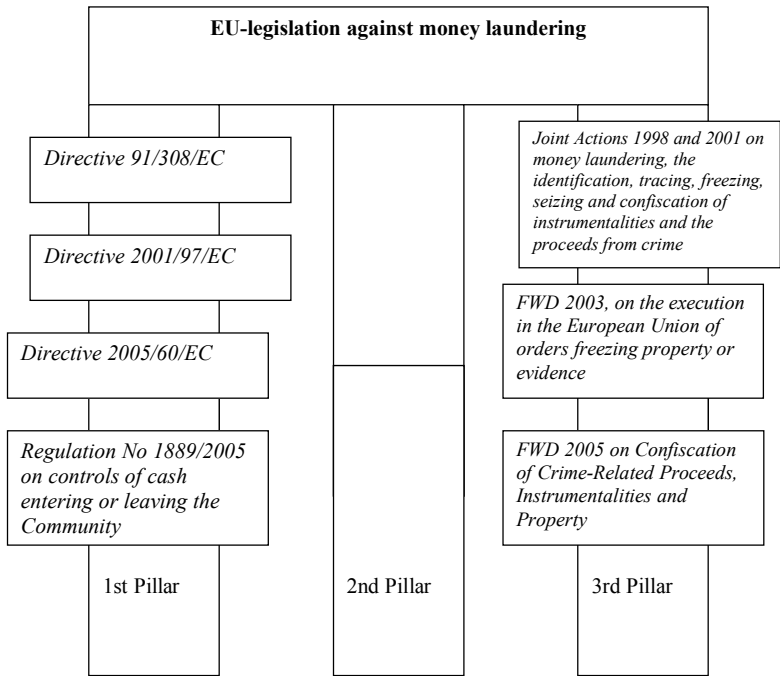


Figure 1 EU-legislation against money laundering

But why the EU has used so many different legal instruments? In the third pillar the instruments available for use are different compared to the first pillar. In the first pillar Directives and Regulations are used. The Article 249 EC Treaty provides that ‘*A directive shall be binding, as to the result to be achieved, upon each Member State to which it is addressed, but shall leave to the national authorities the choice of form and methods*’, whereas ‘*A regulation shall have general application. It shall be binding in its entirety and directly applicable in all Member States*’. Furthermore according to Article 34(2) EU Treaty, FWDs, successors of Joint Actions, are used to approximate laws and regulations of the Member States being binding on the Member States as to the result to be achieved but leave the choice of form and methods to the national authorities.

So from above it can be concluded that FWD are used in the third pillar because they are the only legal instruments which can be used under that pillar. But why Directives are so widely used in regulating the money laun-

dering under the first pillar? The most important explanation for this is the EC's competence to criminalise; when issuing those Directives, the EC had no competence to demand the Member States to criminalise any act and thus it had to rely on Directives. The other explanations are that the demands set out in the AML Directives, at least in the third Directive, are pretty detailed, the Member States have different legal systems and some of the Member States had already more regulated money laundering than others. So, thus the Directives were regarded as the best tools under the first pillar to address those kinds of problems.

The aim of AMLS introduced by this double text approach by the EU was to harmonise the laws of the Member States regarding the money laundering. The main purpose was to criminalise the money laundering. This criminalisation happened in a form of Directives. Adoption these Directives is a condition of entry for all new EU Member States. Because the Member State, not strictly applying the Community Directives, would be the weakest link in the point of view of money launderers (the *balloon theory*) and that country could also erode the economy of the whole EU by allowing the launderers to enter into internal market area.¹⁴⁹ However, the application of Directives is still based on national concepts and standards of interpretation which can make them less effective legal instruments.

6.3.1 Joint Actions, Framework Decisions and Regulations

FWDs and Joint Actions under the EU's AML regime are mainly targeted to freezing, tracing, seizing and confiscation of proceeds of crime and to improve co-ordination between countries. The most important regulation in the EU's AML regime is the *Regulation (EC) No 1889/2005 of the European Parliament and of the Council of 26 October 2005 on controls of cash entering or leaving the Community*¹⁵⁰. In this chapter above mentioned instruments, Joint Actions, FWDs and Regulations, are discussed.

*A Joint Action 98/699/JHA of 3 December 1998 on money laundering, the identification, tracing, freezing, seizing and confiscation of instrumentalities and proceeds from crime*¹⁵¹ arose from the initiative of the UK. The purpose of the 1998 Joint Action was to improve co-ordination between law enforcement authorities and to improve the potential for disrupting organised

¹⁴⁹ See, above Zagaris' *balloon theory* and D Hopton, *Money Laundering: A Concise Guide for All Business* (Aldershot, Hants, English; Burlington, VT: Gower 2006) 25

¹⁵⁰ OJ L 309, 25.11.2005

¹⁵¹ OJ L 333, 9.12.1998. A number of provisions of the Joint Action were repealed by the 2001 Council FWD; only the currently operative provisions of the Joint Action are discussed here.

criminal activity by more effective co-ordination between Member States in relation to assets derived from crime¹⁵². The 1998 Joint Action recognised that mutually compatible practices were making co-operation at the EU level more efficient and by referring to *the 1997 High Level Group Action Plan on Organised Crime* it emphasised the need to improve procedures for judicial co-operation in relation to OC¹⁵³. The Joint Action demands that each Member State ensures that its legislation and procedures enable it to permit the identification and tracing of suspected proceeds from crime at the request of another Member State where there are reasonable grounds to suspect that a criminal offence has been committed¹⁵⁴ and obligates Member States to encourage direct contact between investigators, investigating magistrates and prosecutors of Member States and to take all necessary steps to ensure that assets which are the subject of a request from another Member State can be frozen or seized expeditiously¹⁵⁵. This Joint Action can be seen to have been strongly influenced by the Council of Europe's *Convention on Laundering, Search, Seizure and Confiscation of the Proceeds from Crime* and 40 Recommendations by the FATF.

The purpose of the *Council Framework Decision 2003/577/JHA of 22 July 2003 on the execution in the European Union of orders freezing property or evidence*¹⁵⁶ is to strengthen and supplement the provisions of the Joint Action 98/699/JHA in accordance with the conclusions of the Tampere European Council 1999. Under the FWD, the Member States will take all measures necessary to avoid expressing or maintaining reservations concerning Articles 2 and 6 of the 1990 Council of Europe Convention. Because it is not always possible to confiscate the proceeds of crime, the FWD provides for the introduction into the legislation of Member States of the possibility of confiscating goods of an equivalent value to the proceeds from crime through internal procedures, procedures initiated at the request of another Member State and requests for the enforcement of confiscation orders issued abroad.

*Council Framework Decision 2005/212/JHA of 24 February 2005 on Confiscation of Crime-Related Proceeds, Instrumentalities and Property*¹⁵⁷ refers to Tampere meeting and 2000 Action Plan. It aims to improve and to

¹⁵² Recitals 10 and 12 to the Preamble to the 1998 Joint Action (OJ L 333, 9.12.1998)

¹⁵³ Recitals 13 and 14 to the Preamble to the 1998 Joint Action (OJ L 333, 9.12.1998)

¹⁵⁴ Article 1 of *Joint Action of 3 December 1998 on money laundering, the identification, tracing, freezing, seizing and confiscation of instrumentalities and proceeds from crime* (OJ L 333, 9.12.1998)

¹⁵⁵ Articles 4 and 5 of *Joint Action of 3 December 1998 on money laundering, the identification, tracing, freezing, seizing and confiscation of instrumentalities and proceeds from crime* (OJ L 333, 9.12.1998)

¹⁵⁶ *OJ L 196*, 2.8.2003

¹⁵⁷ OJ L 68, 15.3.2005

approximate national provisions governing seizures and confiscation of the proceeds of crime. According to the FWD, the existing instruments in the area have not achieved a sufficient level of cross-border co-operation regarding confiscation. According to the FWD, Member States shall take necessary measures to enable confiscation of proceeds of certain crimes. The aim of the FWD is to ensure that all Member States have effective rules governing the confiscation of proceeds from crime, inter alia in relation to the onus of proof regarding the source of assets held by a person convicted of an offence related to organized crime. FWD in its preamble refers to Vienna Action Plan, the UN Conventions as well as Council of Europe Convention, that all have previously laid a foundation stone in the field of tracing, freezing, confiscation and seizure.

Regulation No 1889/2005 on controls of cash entering or leaving the Community places an obligation on any natural person entering or leaving the Community and carrying cash of a value of EUR 10 000 or more to declare that sum to the competent authorities. It also demands that the information obtained either from the declaration or as a result of controls must be made available to the authorities responsible for combating money laundering or terrorist financing in the Member State of entry or of exit. The Member States must also lay down the penalties applicable in the event of failure to comply with the obligation to declare. This Regulation aims to prevent smuggling currency across the borders and thus targets the very nature of the money laundering crime – its transnational character. The regulation is founded on the point 9 *Council Conclusions on making the fight against financial crime more effective*¹⁵⁸ which called for some sort of regulation by stating that ‘*recognizing that the surveillance of cross-border cash flows can improve the effectiveness of the daily struggle against money laundering*’. The regulation does not apply to movements between Member States but it supplements the AML Directives regulating the cash leaving and entering the EU.

Next the look is taken into the most important legislative instruments used in the EU’s AMLS in the fight against money laundering.

6.3.2 First Anti-Money Laundering Directive – an Attempt to Lay the Foundation Stone

In 10 June 1991 *the First European Directive on Prevention of the Use of the Financial System for the Purpose of Money Laundering*¹⁵⁹ was adopted with

¹⁵⁸ *Council Conclusions on making the fight against financial crime more effective*. ECOFIN/JHA meeting on 17 October 2000. Council Doc 12128/00

¹⁵⁹ *OJL 166, 28.6.1991*. Directive 91/308/EEC obliged both EU and EEA countries.

implementation period by January 1993. The Directive with its preventive approach was an important although a small step in the EU's money laundering combat; in practice it introduced only some minimum requirements to be implemented by the Member States. Although the Directive contained many important provisions which have paved the road for the subsequent AML Directives and helped in the fight against money laundering, the Directive was by no means a perfect legal instrument e.g. it left to Member States to choose whether to use criminal law or administrative law to implement the directive.

The Directive had three clear objectives. Firstly, the Directive established the EC as *a transnational security actor* by containing both regulatory and criminal law provisions but because of criminal law competences fell out from EC's competence *Article 2* was included the wording "*Member States shall ensure that money laundering as defined in this Directive is prohibited*".¹⁶⁰ All the Member States were thus required to introduce legislation which made money laundering a criminal offence. The Directive combines criminalization, like used in UN Conventions, and prevention policies, like the FATF, thus reflecting the acknowledgement of the close interrelation of the goals of penal deterrence and protection of the financial system.

The Directive was introduced in the 1990's when the protection of financial institutes was seen to have the utmost importance. The Directive was dedicated to protect of financial institutes which were seen to play a crucial role in European wide economy. The aim of the Directive was to prevent of the use of the financial system for money laundering purposes and to guarantee a proper functioning of the economic and financial transactions. The Directive based on the 40 Recommendations of the FATF¹⁶¹ also made references to the Vienna Convention and Strasbourg Convention.

According to the Directive, '*criminal activity*' means a crime specified in *Article 3(1) (a)* of the Vienna Convention and any other criminal activity designated as such for the purposes by each Member State. It was commonly argued that the AMLS adopted in this Directive was too flexible; the predicate offences covered by the Directive should had included whether the proceeds of all organised crime or at least a catalogue of predicate offences, like drug trafficking, terrorism, illegal gambling, trafficking in human beings

¹⁶⁰ Not that Member States shall "*ensure that money laundering is treated as a criminal offence*" as originally was suggested. There has been lots of arguments insisting that the wording taken to the Directive could have watered-down the whole Directive unless the Member States were not obligated to implement the Directive. K Magliveras, 'The European Community's Combat Against Money Laundering: Analysis and Evaluation' (1998) 5 *Nova Southeastern University ILSA Journal of International & Comparative Law* 91

¹⁶¹ EU is a member of the FATF. M Pellegrini, '*Anti-Money Laundering Legislation in the Light of the Proposal of the Third EC Directive 2005*' (2005) 16 *E.B.L.Rev.* 1181

and prostitution, and the Member States had been left free to add that list.¹⁶² Although it was considered that the adoption of this kind of list could bring more unity and clear the concepts¹⁶³ and thus make the deterrence effect of criminalization of the money laundering more effective, the list cannot ever be exhaustive. This was, however, defect which was closely considered in drafting further Directives.

Articles 3-10 required credit and financial institutions to facilitate the criminal investigation of money laundering by RSTs and transactions above €15 000 threshold. To be able to prevent ‘*smurfing*’, also the transactions under €15 000 appearing to be loosely connected were put subject to identification.¹⁶⁴ Using this kind of pluralisation/responsibilisation strategy, making certain actors in the society to act as pro-active agents in prevention of money laundering, and emphasising on the most vulnerable phase in the money laundering operation, the placement stage, the Directive obligated financial institutions and insurance companies¹⁶⁵ to verify their customers’ and beneficial owners’ identification (*KYC* -strategy) when entering into business relations¹⁶⁶ and to keep adequate records of transactions and identification for at least five years.

The Directive can be seen to be built upon the traditional approach, the Three Stage -model – assuming that money launderers deposit cash into financial institutions, as happens at the placement stage in the traditional model. However, one thing which was a clear defect was that the Directive did not include any provision which could have made the failure to report about transactions above threshold a criminal offence on the part of the employees and the offence of corporate crime in the part of the financial institution.

The Directive can be seen to lack specific provisions relating to the customers’ and beneficial owners’ identification, although financial institutions were obligated to verify their customers’ identity, the Directive did not give any details on the relevant procedures, how this identification was to happen in practise. There was also no detailed definition of the term beneficial owner. A clear shortcoming in the Directive is also that if the client of financial institution was personally known to the bank and his identity had already

¹⁶² K Magliveras, ‘*The European Community’s Combat Against Money Laundering: Analysis and Evaluation*’ (1998) 5 *Journal of International & Comparative Law* 91 and OJ No C 198, 8.7.1996; Appendix 2 to Second Commission Report to the European Parliament and Council on the Implementation of the Money Laundering Directive COM (1998) 401 final

¹⁶³ M Sideek, *European Community Law on the Free Movement of Capital and the EMU*. (London, Kluwer Law International 1999) 173-175

¹⁶⁴ Article 3 in Directive 91/308/EEC

¹⁶⁵ Some exclusions in Article 3(3) and (4) in Directive 91/308/EEC

¹⁶⁶ For example opening a bank account or setting up a deposit box. Article 3 in Directive 91/308/EEC

been established, the financial institution in question did not have to obtain any evidence of his identity. Thus an old client of bank turning to be a money launderer could have escaped the money laundering checks.

This pluralisation/responsibilisation strategy, the second objective of the Directive, put lot of pressure on financial institutions both economically and morally. The strategy made the persons behind the counter to become moral filters. The Directive also required the institutions to implement and maintain adequate internal controls and staff training to ensure that the staff are aware of the law and are trained to spot potentially suspicious transactions. However, the Directive made no reference to the employees' qualifications; there was no need for proof of no prior convictions as a qualification required for membership the legal professionals either. Thus it would have been possible that a person with previous convictions of money laundering could have worked as a key employee in some financial institution and thus to facilitate money laundering in the institution.

It is argued that the strategy of compulsory reporting of all transactions involving a minimum amount (certain threshold) has not been particularly effective because it is easy to play safe and make deposits worth of much less than the threshold¹⁶⁷. The fact is that the amount of the transactions, valued €15 000 or more, occurring is so great that it is impossible to authorities to detect all the reported transactions. Also the reporting, concerning the suspicious transactions, is made on subjective basis which may make it very unreliable; term '*suspicious transaction*' was not even defined in the Directive but it is left to be defined by the Member States themselves and can be seen more often to be based on national and cultural stereotypes than well-founded concerns. Thus the decision to report may be based on a gut feeling rather than concrete evidence.

Because it was known that money launderers do not use mere financial institutions to launder their illegal proceeds, the *Article 12* encouraged the Member States to cover under their national AML legislation also other forms of activity¹⁶⁸ that were considered to have a risk of handling illegal money. Thus, this piece of the strategy created some considerable disparities between different jurisdictions, for instance in UK and Germany insurance businesses were covered while in the Netherlands also casinos and credit card companies¹⁶⁹. **It is generally argued that the Directive provided inadequate protec-**

¹⁶⁷ K Magliveras, 'The European Community's Combat Against Money Laundering: Analysis and Evaluation' (1998) 5 *Journal of International & Comparative Law* 91

¹⁶⁸ Other than the credit and financial institutions referred to in *Article 1* in Directive 91/308/EEC.

¹⁶⁹ M Sideek, *European Community Law on the Free Movement of Capital and the EMU*. (London, Kluwer Law International 1999) 174

tion to the non-financial institutes because while increasing the controlling and reporting of the customers of financial institutions it forced ‘*smurfs*’ to explore opportunities outside the banking system. This was seen a general shortcoming that the scope of Directive did not specially cover post offices, casinos, real estate agents, art dealers and precious metal dealers.

The prevention strategy was mostly seen in *Article 6* which touched a nerve by lifting banking secrecy, as the third objective of the Directive. Financial institutions were no more allowed to hold anonymous bank accounts¹⁷⁰. This prohibition harmonised the banking practices of the Member States at the certain extent e.g. by abolishing Sparbuch accounts¹⁷¹. However, the imposed duty for financial institutions to supply information about their customers was seen to be in conflict with the banks’ duty of customers’ confidentiality.

The prevention strategy is also seen in *Article 8* which ruled out so called *tipping off*-principle; the suspects of money laundering were banned from being cautioned that they are being investigated and anyone reporting a suspicion was ordered to be protected from actions from breach of confidence. *Article 9* even concludes that any disclosure, done in good faith to the competent authorities, shall not involve civil or penal responsibility on the part of institution or its employees that disclosed the sensitive information. This may have caused false STRs because the threshold of institutions of reporting suspicious transactions is made low, institutions do not have to fear the punishment resulting from false reporting, actually they are really encouraged to report. Maybe because it is known that institutions may be reluctant in reporting because it causes extra work for them.

The Directive was caught in the crossfire through the Community – although various trade bodies and legal professionals saw the Directive correspond the real life needs, it was also criticised being too flexible and too much a product of compromise¹⁷². The major concern was however whether the EU had competence to demand the Member States to criminalize certain acts and to impose criminal sanctions for certain acts. More discussion about the EU’s competence in the criminal matters and problems relating to flexibility of Directives is found in the chapter 7.

The inability of the Directive to prevent the encroachment of criminals

¹⁷⁰ In 2000 the banking secrecy matter was took even further, Convention on mutual assistance on criminal matters between the Member States of the EU (OJ 2000 C 197/1) placed obligations on member states to provide information on bank accounts and transactions and removed some of the grounds on which Member States could refuse to cooperate with requests.

¹⁷¹ For more discussion, see P Lilley, *Dirty Dealing: the Untold Truth about Global Money Laundering, International Crime and Terrorism* (Kogan Page, Sterling 2006)

¹⁷² M Sideek, *European Community Law on the Free Movement of Capital and the EMU*. (London, Kluwer Law International 1999) 173

into the securities market, which was commonly used at the layering stage,¹⁷³ as well as the Directive's lack of more co-ordinated approach in co-operation between the regulatory and the law enforcement authorities,¹⁷⁴ including central reporting units, were emphasised¹⁷⁵ because of the recommendations by the Egmont Group. Because the Directive did not include any provisions allowing the competent authors in one Member State to request the transmission of information from another Member State relating to money laundering investigations, it did not thus enough concern the cross boarders cash flows, typical for money laundering operations. Furthermore, the reporting requirements were seen to need some extension. Although it was argued that the financial institutions had some advantages from this Directive like protection of their image and shielding them from acts of fraud,¹⁷⁶ the opposite opinions were also cast. One of the major concerns was whether the Directive requiring information for security reasons and setting aside the individual privacy rights has gone too far. Questions, how far should legislation go in requiring details of financial transactions and which organisations should be subject to these requirements, were cast¹⁷⁷.

Seven years after *Second Commission Report to the European Parliament and Council on the Implementation of the Money Laundering Directive* called for an extension of the rules to cover the legal professions as well as it expressed concern as to non-financial institutions not yet covered by regulations. Behind this idea were the revised 40 Recommendations by the FATF issued in 1996. This report also called for application of KYC –principles in the situations where, because of Internet or other medium, there is no face-to-face contact¹⁷⁸. It was time for the second AML Directive to burst upon the EU's AML scene.

¹⁷³ Ibid 174

¹⁷⁴ K Magliveras, 'The European Community's Combat Against Money Laundering: Analysis and Evaluation' (1998) 5 *Journal of International & Comparative Law* 91

¹⁷⁵ First Commission report on Money Laundering Directive COM(95)54 final Brussels 3 March 1995. Furthermore, EU Council of Ministers' decision of October 2000 concerning arrangements for cooperation between financial FIUs of the Member States (2000/642/JHA) tried to improve the cooperation between contact points competent to receive STRs pursuant to Directive 91/308/EEC

¹⁷⁶ Ibid

¹⁷⁷ 'Blanchiment d'argent' (An article on the website EurActiv.com 17.3.2006) <<http://www.euractiv.com/fr/services-financiers/blanchiment-argent/article-140992>> (accessed 28.8.2008)

¹⁷⁸ Second Commission Report to the European Parliament and Council on the Implementation of the Money Laundering Directive COM (1998) 401 final

6.3.3 The Amending Directive – Filling the Gaps

The 1991 Directive was extended and updated by *Directive 2001/97/EC of the European Parliament and of the Council of 4 December 2001 amending Council Directive 91/308/EEC on prevention of the use of the financial system for the purpose of money laundering*¹⁷⁹ (referred as the amending Directive). The amending Directive was planned to reflect the best international practice in the area¹⁸⁰ but in reality it just filled the gaps left by the previous Directive, concentrating mainly on the placement stage of the money laundering process and to detect only the less well sophisticated ways of money laundering.

The amending Directive, making a reference to the 1996 revised 40 Recommendations by the FATF, emphasised the importance of the wider range of predicate offences.¹⁸¹ It had four main objectives¹⁸²: firstly, it obligated the Member States to criminalise the money laundering of proceeds resulting from serious crimes, like the drug trafficking offences, activities of criminal organisations, serious fraud, corruption and any offence which may generate substantial proceeds and which is punishable by severe sentence of imprisonment in accordance with the penal law of the Member State¹⁸³ but it did not contain any precise definition of serious crime, only some examples of what may constitute a serious crime.

The amending Directive like the previous one was aimed especially to ensure the stability and integrity of the Member States' financial systems. The second aim of the amending Directive was to widen the pluralisation/responsibilisation strategy – to extend the duties of identification, registration and reporting also to non-financial agents likely to be involved in money laundering. *Article 2* brought in addition to credit and financial businesses (which were extended to include e.g. investment firms) also the non-financial businesses, like estate agents, auditors, casinos, dealers in high-value goods, notaries/other independent legal professions participating in specified functions and auctioneers, under the umbrella of the Directive.¹⁸⁴

Article 6 contained both proactive and reactive reporting obligations subjecting legal professionals to obligations¹⁸⁵; it extended also the obligations of the customer identification, record keeping and RSTs to some acti-

¹⁷⁹ OJ L 344, 28.12.2001. Directive 2001/97/EC was to be implemented by the Member States by June 2003

¹⁸⁰ Recital 1 in the preamble in Directive 2001/97/EC

¹⁸¹ Recital 7 in the preamble in Directive 2001/97/EC

¹⁸² M Pellegrini, 'Anti-Money Laundering Legislation in the Light of the Proposal of the Third EC Directive 2005' (2005) 16 E.B.L.Rev. 1181

¹⁸³ Article 1(e) in Directive 2001/97/EC

¹⁸⁴ Articles 1 and 2 in Directive 2001/97/EC

¹⁸⁵ Article 6(3) in Directive 2001/97/EC

vities and professions e.g. lawyers which have been shown to be vulnerable to money laundering. This strategy and *Article 6* raised fundamental rights concerns¹⁸⁶ and thus it was determined that reporting obligations under the amending Directive should not apply to independent professionals providing legal advice where they were ascertaining the legal position of a client or representing client in legal proceedings – ‘it would not be appropriate... to put these legal professionals in respect of these activities under an obligation to report suspicions of money laundering’¹⁸⁷.

Article 3(11) extended the KYC -strategy, the third objective of the amending Directive, obligating the Member States to ensure that the specific and adequate measures, e.g. requirement of providing additional documentary evidence or supplementary measures to verify/certify the documents supplied, are taken to compensate the greater risk of money laundering which arises in non-face-to-face, transactions. It also made it obligatory to identify all casino customers purchasing or selling gambling chips with a value of €1 000 or more,¹⁸⁸ however, failing to define whether also private members’ casinos were under this obligation¹⁸⁹.

The amending Directive created one major and a brand new piece of AMLS by obligating all the Member States to establish FIUs¹⁹⁰ to which STRs were to be made. This *centralised information management* can be seen as fourth aim of the amending Directive. The FATF and the Egmont Group can be seen to be behind this idea of the creation of the FIUs. However, FIUs took different forms in different jurisdictions and these forms created barriers to the exchange of information¹⁹¹. The different forms of FIUs were, however, not the only obstacle in the way of harmonising AML legislation in the Member States.

Furthermore, as emphasised in the preamble, the aim of the amending Directive was also to protect public morals.¹⁹² The amending Directive did not add any new justifications for the fight against money laundering; it only

¹⁸⁶ The European Court of Justice ruled that the amending Directive was compatible with the right to a fair trial in Article 6 of the ECHR and Article 6(2) of the Treaty on European Union following a request from the Belgian Bar Association in 2005. ‘Blanchiment d’argent’ (An article on the website EurActiv.com 17.3.2006) <<http://www.euractiv.com/fr/services-financiers/blanchiment-argent/article-140992>> (accessed 28.8.2008)

¹⁸⁷ Recitals 17 in the preamble in Directive 2001/97/EC

¹⁸⁸ Article 3(5) in Directive 2001/97/EC

¹⁸⁹ J Handoll, *Capital, Payments and Money Laundering in the European Union* (Dublin, William Fry 2006)

¹⁹⁰ 2000/642/JHA had already tried to improve the cooperation between contact points competent to receive STRs pursuant to Directive 91/308/EEC

¹⁹¹ Article 10 in Directive 2001/97/EC and A Rizkalla, ‘*Money Laundering: the European Approach*’ (1998) 13 Tulane Euro Civ LF 111

¹⁹² Recitals 2 and 14 in the preamble in Directive 2001/97/EC

concluded that money laundering should be prevented ‘for prudential reasons’¹⁹³. Worth of noticing is also the wording ‘*measures should not impose restrictions that go beyond what is necessary to achieve those objectives*’¹⁹⁴. This wording gave lots of space, i.e. what actually constituted ‘*necessary*’ – should it be concluded by using cost-benefit analysis, the benefits of certain Member State(s), the financial institutions, the actors subject to the Directives or the EU itself?

The commitment within the amending Directive not to legislate further until an evaluation had been carried out was not respected. Indeed the European Commission made, in 2004, a proposal to update and to improve the existing AMLS, aiming to strengthen the EU’s defences against money laundering and to prevent terrorist financing and at the same time to adopt the 2003 revision of the 40+9 Recommendations of the FATF¹⁹⁵. The third Directive was adopted on 20 September 2005. However, the general opinion has been that the third Directive has been premature and inappropriate because some of the Member States were not yet even implemented the amending Directive¹⁹⁶.

6.3.4 *The Third Directive – the New Direction*

*“We have agreed on a good compromise [the third Directive], which prevents the new rules from turning into an unnecessary bureaucratic exercise.”*¹⁹⁷

Directive 2005/60/EC of the European Parliament and of the Council of 26 October 2005 on the prevention of the use of the financial system for the pur-

¹⁹³ Recital 2 in the preamble in Directive 2001/97/EC

¹⁹⁴ Recital 2 in the preamble in Directive 2001/97/EC

¹⁹⁵ ‘Money laundering: Commission proposes to update and improve Directive’ (30 June 2004) EU Doc IP/04/832 <www.europa.eu.int/rapid/pressReleasesAction.do?reference=IP/04/832&format=HTML&aged=1&language=EN&guiLanguage=en> (accessed 30.6.2008)

¹⁹⁶ ‘Money Laundering’ (An article on the website EurActiv.com 27.5.2005) <<http://www.euractiv.com/en/financial-services/money-laundering/article-139944>> (accessed 2.8.2008)

¹⁹⁷ Nassauer H, ‘*European Parliament for tougher measures on money laundering*’ (The press release of the EPP-ED group in the European Parliament 26.05.2005) <<http://www.epp-ed.org/Press/showpr.asp?PRControlDocTypeID=1&PRControlID=3705&PRContentID=6889&PRContentLG=en>> (accessed 4.8.2008)

pose of money laundering and terrorist financing¹⁹⁸, (referred as the third Directive), which had an adaptation period of two years, by 25 November 2007, aims both to protect and to maintain stability and reputation of the financial sector and the single market and to criminalise the financing of terrorist activities.¹⁹⁹ *Article 37* states the need for efficient enforcement and supervision while *Article 39* introduces sanctions including administrative sanctions. This Directive can be argued to mirror almost totally the new global AML standards set in 2003 by the FATF. Some exceptions can however be found, like the Directive does not grant the Commission a mandate to establish a binding list, ‘*White list*’²⁰⁰, of countries which have equivalent AML legislation.

The third Directive, as its predecessors, takes a preventive approach to money laundering problem. It sees the use of criminal law at the national level as an inadequate and non-uniform response adopting a co-ordinated response at Community level²⁰¹ “...in accordance with the principle of subsidiarity as set out in Article 5 of the [EC] Treaty”²⁰².

The definition of money laundering²⁰³ goes beyond the FATF requirements by bringing under its scope all persons dealing in goods or providing services for cash payment of €15 000 or more. The third Directive broadens the existing categories of the bodies covered by bringing trusts and company service providers and Internet transactions within its scope²⁰⁴. Although the third Directive can be seen to depart from the Three Stage -model and to accommodate, at least to some extent, the Chameleon theory, the fact is that the use of large cash payments in the 21st century has reduced significantly – it can be argued that the launderers may prefer electronic form of money instead of cash. Although taking the Internet transactions under its scope, the third Directive can be argued to provide no effective means to root out ‘*cyber laundering*’ e.g. the money laundering service providers on Internet.

According to the Directive culpability could be constructed on the basis of objective facts. That leaves room for national implementation. Interesting is also that Art 1(2)(b) of Directive accommodates the classic common law

¹⁹⁸ *OJL 309, 25.11.2005*. Amended by Directive 2008/20/EC of the European Parliament and of the Council of 11 March 2008 amending Directive 2005/60/EC on the prevention of the use of the financial system for the purpose of money laundering and terrorist financing, as regards the implementing powers conferred on the Commission. *OJL 76, 19.3.2008*

¹⁹⁹ Article 1(1) in Directive 2005/60/EC

²⁰⁰ BakerPlatt Chairman Questions EU Money Laundering ‘White List’, by Jason Gorringer, (An article on the website Tax-News.com)

<http://www.tax-news.com/asp/story/BakerPlatt_Chairman_Questions_EU_Money_Laundering_White_List_xxxx31468.html> (accessed 29.9.2008)

²⁰¹ Recital 1, 2 and 3 of the preamble in Directive 2005/60/EC

²⁰² Recital 46 in the Preamble in Directive 2005/60/EC

²⁰³ Article 1(4) in Directive 2005/60/EC

²⁰⁴ Recitals 14-8 in the Preamble in Directive 2005/60/EC

offences of attempt, conspiracy and incitement. There can also be found references to complicity i.e. aiding, abetting, facilitating and assisting in the Directive. The Directive also prohibits possession of laundered money.

The main changes in the AMLS are set out in Articles 7-13 of the third Directive. Article 7 introduces a new generation of the KYC –strategy, containing more detailed requirements for customer due diligence (CDD). These CDD –principles are founded on the Wolfsberg principles and the FATF’s 40+9 Recommendations. These articles tried to meet the needs of the financial sector because the financial sector has long complained that the burden placed on them in the fight against money laundering is already unreasonable. They see KYC -rules to place an onerous burden on law firms, especially because the overwhelming percentage of customers is seen not to pose any threat with respect to money laundering.

In order to reduce the workload in many routine cases and to implement the idea that AMLS should be proportionate²⁰⁵ to the risks involved, Articles 8-13 of the third Directive introduced the concepts of risk assessment and risk management to EU’s AMLS. This, risk-based approach²⁰⁶, having its origin in the Wolfsberg principles, demands the actors covered by the Directive to apply CDD measures ‘*on a risk-sensitive basis depending on the type of customer, business relationship, product or transaction*’ and to ensure that ‘*the extent of the measures is appropriate in view of the risks of money laundering*’²⁰⁷. Two main risk categories, a low and a high risk category, are also introduced. These categories can be seen to give firms some leeway as to how they implement the risk-based approach. Because it would be waste of time and money to carry out a careful CDD on very large, stock exchange companies, like Nokia, so these kinds of companies could be subject to simplified CDD. However, the CDD requirements do not disappear in any case – it can be argued that there may not be any reduction in the workload of the financial institutions. There is also now need to apply a case by case approach to the different categories of customers/transactions²⁰⁸. A risk-based approach is also unlikely to be cheaper to operate than the previous approach and will involve start-up costs.

The major difference between the third Directive compared to the previous ones is the total change of the approach from the strict all-embracing,

²⁰⁵ Recital 41 in the Preamble in Directive 2005/60/EC

²⁰⁶ Recital 22 in the Preamble in Directive 2005/60/EC

²⁰⁷ Article 8(2) in Directive 2005/60/EC

²⁰⁸ British bankers association comments on Commission working document of 12 September 2005 on implementation of 3rd money laundering directive.

<http://forum.europa.eu.int/Public/irc/markt/markt_consultations/library?l=/financial_services/financial_crime/30_bba_enpdf/_EN_1.0_&a=d> (accessed 19.7.2008)

'all or nothing' -strategy, found in the two previous Directives, to the risk-based approach found in this third Directive. The main weakness of the 'all or nothing' -strategy has been the reporting (STRs) overload²⁰⁹. Whereas by placing a high responsibility to the institutions and the persons covered by the third Directive, e.g. *Article 8* requires the establishment of the purpose of the business relationship and its intended nature and requires the relationship to be monitored on an ongoing basis in order to ensure that it remains within the originally stated purpose, the risk-based approach provides a basis for reducing the amount of reports because it enables the actors subject to the regulations to have greater flexibility, enabling lot of discretion, in responding the complex problem of money laundering.

The risk-based approach provides more room for to decide whether the activity needs to be reported and it can also be argued that the financial institutions have already lots of experience in the management of risks, but the problem is that the non-financial institutions and other actors may not have any experience in that field. However, regarding the financial institutions, this can be a double edged sword: risk-based measures may only be transferred from the management of other kinds of risks and thus, as a result, private actors and regulators can approach the problem in different ways²¹⁰. The risk-based strategy requires the analysing the risks in more careful terms than in past. The effectiveness of it can be evaluated balancing how well it targets high risk activity while at the same time avoids putting barriers in the way of legitimate financial active²¹¹ – the aim of this is that financial activity on an occasional or limited basis and where there is little risk of money laundering, does not fall in the scope of the Directive²¹². It can also be impugned how eager the institutions are to monitor transactions of already established customers – questions arise about the costs of such monitoring and the availability of staff. The main challenge is thus to avoid '*window dressing*' and to ensure the effective application of the CDD –principles in practise. A general comment on these criteria is that these criteria are complex and will be difficult for firms to reach agreement on which situations will be covered by them. Fewer and clearer criteria would be preferable²¹³. By establishing this pluralisation/responsibilisation strategy, the emphasis should be put on the training of

²⁰⁹ S Ross and M Hannan, '*Money laundering regulation and risk-based decision-making*' 2007 10(1) J.M.L.C. 106

²¹⁰ Ibid

²¹¹ Ibid

²¹² Article 2(2) in Dir 2005/60/EC

²¹³ British bankers association comments on Commission working document of 12 September 2005 on implementation of 3rd money laundering directive.
<http://forum.europa.eu.int/Public/irc/market/market_consultations/library?l=/financial_services/financial_crime/30_bba_enpdf/_EN_1.0_&a=d> (accessed 19.7.2008)

e.g. front line staff like clerks and cashiers in the detention and identification process²¹⁴. Of course one option for companies is to rely on third parties, to outsource compliance work, but at the same time that increases costs.

Those actors covered by the third Directive have now to concentrate their efforts on the higher risk situations and should not needlessly duplicate customer identification procedures by allowing customers to be introduced whose identification has been carried out elsewhere²¹⁵. One feature of this new generation of AMLS is that stricter checks are required where the risk of money laundering is higher, e.g. where the customer has not been physically present, like the activities performed on the Internet²¹⁶ or in relations with PEPs i.e. individuals holding important public positions, their direct relatives or persons known to be close associates or '*immediate family members*'²¹⁷. It is not mentioned in which jurisdiction the person may have held such office: the concept of 'high-risk' jurisdictions or governments is absent. It is arguable that the same scrutiny is in fact as necessary for the accounts of prominent figures from the Member States as for those of other jurisdictions, given the past political scandals there²¹⁸. The definition of PEPs²¹⁹ also creates potential problems – it contradicts the risk-based financial approach, in that it includes everyone, not just those posing a genuine risk²²⁰. Also question what are '*prominent public functions*' can be cast²²¹. It is also suggested that the risks of money laundering in relation to frauds (notably against the EU's financial interests) – e.g. in relation to MEPs and officials in the Commission, so the category '*Politically and Financially Exposed European Persons*' (PFEEPs)

²¹⁴ M Sideek, *European Community Law on the Free Movement of Capital and the EMU*. (London, Kluwer Law International 1999) 173

²¹⁵ Recital in the Preamble 27 in Directive 2005/60/EC

²¹⁶ Article 13(2) in Directive 2005/60/EC

²¹⁷ Article 3(8) in Directive 2005/60/EC

²¹⁸ A Richard, 'Reputational issues arising under the EU third money laundering directive' (2006) 27(12) Co Law 373

²¹⁹ Commission Directive 2006/70/EC of 1 August 2006 laying down implementing measures for Directive 2005/60/EC of the European Parliament and of the Council as regards the definition of PEP and the technical criteria for simplified CDD procedures and for exemption on grounds of a financial activity conducted on an occasional or very limited basis. This Directive contains the technical aspects of the definitions given in Directive 2005/60/EC, including that of PEPs (heads of State, heads of government, ministers, members of parliament, etc.). *OJL 76, 19.3.2008*

²²⁰ 'Money Laundering' (An article on the website EurActiv.com 27.5.2005) <<http://www.euractiv.com/en/financial-services/money-laundering/article-139944>> (accessed 2.8.2008)

²²¹ A Richard, 'Reputational issues arising under the EU third money laundering directive' (2006) 27(12) Co Law 373

should be established.²²²

The CDD requirements with especially the provisions regarding PEPs and beneficial owners are regarded to impose higher burdens on firms; financial institutions²²³ argue that the implementation costs place a significant burden on the industry, making especially smaller market participants to suffer²²⁴.

The Council of the Bars and Law Societies of Europe has argued that the reporting provisions of the amending Directive threatened the independence of lawyers and therefore the fundamental right to legal advice and representation.²²⁵ As a respond to this AMLs introduced in the third Directive includes also notion that it respects the fundamental rights recognised by the Charter of Fundamental Rights of the European Union and nothing in the third Directive should be interpreted or implemented in a manner that is inconsistent with the *European Convention on Human Rights*.²²⁶ This statement is a welcomed adjunct; there has been critique because this kind of statement has been missing from the previous Directives. It can, however, be argued that this kind of wording is mere 'window dressing' and does not guarantee that inconsistencies with fundamental rights do not take place.

6.3.5 Related Legislative Instruments

In addition to the AML Directives there exist a number of other EC measures relating to money laundering and terrorist financing. All of these other measures e.g. *Regulation 1889/2005 on information on the payer accompanying transfers of funds* and *Directive 2007/64/EC of the European Parliament and of the Council of 13 November 2007 on payment services in the internal market* are designed to give effect to 40+9 Recommendations by the FATF and are specially aimed to terrorist financing although at some parts they are also relevant to money laundering. Whereas *Directive 2007/64/EC on payment*

²²² N Dorn, 'Re: Invitation of Public Comment: Working document in relation to the Directive of the European Parliament and of the Council on the prevention of the use of the financial system for the purpose of money laundering and terrorist financing' (October 2001) <http://forum.europa.eu.int/Public/irc/market/market_consultations/library?l=/financial_services/financial_crime/criminologist_enpdf/_EN_1.0_&a=d> (accessed 23.8.2008)

²²³ T Buck, 'New money laundering laws put more onus on professions' *Financial Times* (Brussels 27.5.2005) <<http://www.ft.com/cms/s/4457bf4e-ce4d-11d9-9a8a-00000e2511c8.html>> (accessed 29.8.2008)

²²⁴ H Geiger and O Wuensch, 'The fight against money laundering: An economic analysis of a cost-benefit paradox' (2007) 10(1) *J.M.L.C.* 91

²²⁵ -- 'Money Laundering' (An article on the website EurActiv.com 27.5.2005) <<http://www.euractiv.com/en/financial-services/money-laundering/article-139944>> (accessed 2.8.2008)

²²⁶ Recital 48 in the Preamble to the 2005 Directive

services in the internal market provides the legal foundation for the creation of an EU-wide single market for payments aiming to establish a modern and comprehensive set of rules applicable to all payment services in the EU. The Directive demands that institutions should be made subject to effective AML and anti-terrorist financing requirements.

7 STRENGTHS, WEAKNESSES, OPPORTUNITIES AND THREATS OF THE EUROPEAN UNIONS ANTI-MONEY LAUNDERING CRUSADE

*“A penal law drafted to accommodate the diverse interests and prejudices of Member States will turn out to be a weak legal weapon with which to fight crimes, particularly sophisticated financial crime and white collar crimes”.*²²⁷

As seen above, money laundering is a pretty new-born law creature and it has become a motor of international co-operation in financial surveillance²²⁸. In this chapter I have used the SWOT –analysis to evaluate strengths, weaknesses, opportunities and threats regarding the EU AMLS. This SWOT –analysis (figure 2) is widely used in the business world to analyse the projects and business ventures and I have regarded it as a suitable tool to analyse the EU’s AMLS as well.

7.1 SWOT -Analysis

The building of the EU’s AMLS has not taken place without criticism. There have existed major stumbling blocks which have hampered the EU AML crusade. But also the strategy has been at least for some extent successful, for example the EU has recognised the complexity of the phenomenon in the third Directive and there can be seen a trend towards a much wider definition of money laundering based on a broad ranger of predicate crimes and also new concepts, like PEP, are introduced.

However, the complexities of the phenomenon of money laundering and its ‘dark figure’ have caused problems. The phenomenon of money laundering is neither totally known, for example the underground banking systems. This imperfect understanding of the phenomenon has hampered the legislation process and made legislation ineffective regarding certain points. For example Van Duyn²²⁹ claims that after implementing the money laundering legislation in the EU there has been created a new underground money-processing system. Maybe there should also be concerns about the excessive

²²⁷ M Sideek, *European Community Law on the Free Movement of Capital and the EMU*. (London, Kluwer Law International 1999) 172

²²⁸ P Alldridge, *Money Laundering Law* (Hart Publishing, Oxford 2003) 107

²²⁹ P van Duyn, *Money Laundering: Pavlov’s Dog and Beyond*, 37 (1998) *The Howard Journal* 4 359

checks used to prevent money laundering because these checks can harm the competitiveness of financial institutions.

A significant part of AMLS is focused on account opening procedures because the placement stage is still regarded as crucial point for the detection of money laundering operations. However, it is nowadays widely argued that in today's world cash transactions have become largely insignificant and thus the AML Directives have only '*a token effort*' because they have concentrated exactly on those cash transfers²³⁰. The Directives do not either provide means how the customers' identification should take place; thus, the financial institutes may have to rely only on information provided by the customer. The various prevention schemes have also weakened the basic rights of the bank clients, who have to pay for the prevention measures. It is also possible that the AMLS have only rooted out the smallest actors of money laundering because their lack of knowledge and they cannot hire professionals or pay large bribes to financial institutions leaving the play ground to more professional money launderers who are the strongest and most harmful to economy. The SWOT -diagram here illustrates these main Strengths, Weaknesses, Opportunities and Threats of the EU's AMLS. Strengths and Weaknesses are attributes of the strategy; Strengths are helpful and Weaknesses harmful. Opportunities and Threats are external factors; Opportunities are considered to be helpful to achieve objective whereas Threats are considered harmful.

²³⁰ H Hafner cited in the article by W Hetzer, 'Money Laundering and Financial Markets' (2003) 11 Eur.J.Crime Cr.L.Cr.J. 266

| | |
|---|--|
| <p>Strengths</p> <ol style="list-style-type: none"> 1. post C-176/03 and C-440/05 ability to criminalise and to impose criminal sanctions 2. 27 Member States 3. flexibility of the Directives 4. pluralisation/responsibilisation strategy 5. co-operation at the regional level 6. preventive approach to the money laundering problem 7. effective legislation regarding freezing and confiscating assets 8. obligations imposed on financial institutions and designated non-financial businesses and professions 9. proactive and reactive reporting obligations 10. supporting a global strategy 11. a trend towards a much wider definition of money laundering based on a broad ranger of predicate crimes and also new concepts like PEP | <p>Weaknesses</p> <ol style="list-style-type: none"> 1. flexibility of AML instruments 2. not uniform implementation in every Member State 3. rights of privacy 4. imperfect understanding of the phenomenon, e.g. <i>'dark figure'</i> and widely used Three Stage -model 5. exclusive club of <i>'complying countries'</i> 6. <i>'myth of amoral business'</i> 7. the heavy burden of pluralisation/ responsabilisation strategy on financial institutions 8. harm to the competitiveness of financial institutions 9. focus on account opening procedures 10. how the customers' identification should take place 11. only the smallest money laundering actors are rooted out 12. no real means to assess the effectiveness of AMLS |
| <p>Opportunities</p> <ol style="list-style-type: none"> 1. mandatory implementation of AML regime for new Member States 2. the EU can build an effective regional AML regime 3. the EU can act as a role model for other regions 4. OC diminishes | <p>Threats</p> <ol style="list-style-type: none"> 1. there can be created a new underground money-processing system 2. technological changes 3. political developments e.g. establishment of regional trade groupings 4. economic integration 5. more sophisticated OC groups |

Figure 2 SWOT -analysis

As noticed from the SWOT –analysis there exist certain stumbling blocks which can hamper the evolution of the EU’s AMLS. First and the most fundamental one is the question about the criminal law competence of the EU/EC. The second one is the flexibility of the AMLS, the third important point being the effectiveness of the responsabilisation/pluralisation strategy which forces law-abiding actors to become partners in the fight against money laundering. These three points are seen to be the utmost important regarding the EU’s AMLS and are thus discussed next.

7.1.1 Competence to Criminalise or the Absence of It

‘...the Community legislator can, whenever criminal measures are necessary to ensure the full effectiveness of Community law and essential to combat serious offences in a particular area, require Member States to penalise certain conduct and to adopt in that regard effective, proportionate and dissuasive criminal sanctions’²³¹.

Criminalisation of the money laundering can be seen as a cornerstone of EU’s AMLS. The criminalisation of money laundering by the EU/EC can be regarded as problematic. Usually the EC law remains silent on the issue of criminal liability but this has not happened in AML Directives but they make it clear that Member States should prohibit money laundering when committed intentionally. The criminal law has traditionally been seen as a domain of the sovereign nation state and to mirror its identity thus not all of the Member States have been in favour of the strategy; the reluctant attitudes of Luxembourg and the UK have cramped the promulgation of the strategy.

The first Directive names as its legal basis *Articles 47 and 95 TEC*. It can be argued that these provisions do not give the EC any kind of authority to enforce obligations to the Member States to enact criminal legislation. And as Kaiafa-Gbandi²³² puts it *‘it has to be clear that for the Member States no legally binding obligation would arise from the directive 91/308 to undertake special penal measures against money laundering’*. He also continues by remarking that the Member States were not legally bound to implement the first Directive into their internal legal system penalizing the activity of money

²³¹ C- 440/05 Commission v Council loc. cit. note 133 paragraph 112

²³² M Kaiafa-Gbandi, *‘The Development towards Harmonization within Criminal Law in the European Union –A Citizen’s Perspective’* (2001) 9/4 European Journal of Crime, Criminal Law and Criminal Justice 248

laundrying. He emphasizes that the obligation of the Member States through EC Directives to create punishable acts is therefore legally impossible as long as criminal competence has not been conceded to the Community²³³. But the things have changed.

The judgement C-176/03²³⁴ was the watershed. In it the ECJ reiterated the rule that *'neither criminal law nor the rules of criminal procedure fall within the Community's competence'*. But it also held that this rule was only a presumption and it could be overturned. As a result of this judgement it can be stated that in the absence of a general EC power over criminal law *'appropriate measures of criminal law can be adopted on a Community basis only at sectoral level and only on conditions that there is a clear need to combat serious shortcomings in the implementation of the Community's objectives and to provide for criminal law measures to ensure the full effectiveness of a Community policy or the proper functioning of a [internal market] freedom'*²³⁵. These measures may include: the actual principle of resorting to criminal penalties, the definition of the offence and the nature and level of the criminal penalties applicable. According to the judgement, the Community legislature may use the criminal law to achieve its objectives, it may do so only if two conditions are met: *necessity* i.e. any use of measures of criminal law must be justified by the need to make the Community policy in question effective and *consistency* i.e. the criminal law measures adopted at sectorial level on a Community basis must respect the overall consistency of the Union's system of criminal law, whether adopted on the basis of the first or the third pillar. According to this judgement, the Commission has to evaluate case by case whether there is the need to adopt criminal measures at EC level. The Commission has also emphasised that the EC action in criminal law should only be exercised when proved necessary and in the respect of the principles of subsidiarity and proportionality²³⁶. This judgement C-176/03 affects several pieces of legislation since all or some of their provisions were adopted on the wrong legal basis, like *Directive 91/308/EEC on prevention of the use of the financial system for the purpose of money laundering* and *Framework Decision 2001/500/JAI on money laundering, the identification, tracing, freezing, seizing and confiscation of instrumentalities and the pro-*

²³³ M Kaiafa-Gbandi, *'The Development towards Harmonization within Criminal Law in the European Union – A Citizen's Perspective'* (2001) 9/4 European Journal of Crime, Criminal Law and Criminal Justice 239-263

²³⁴ The Lisbon Treaty takes the C-176/03 judgement into the text of the treaty.

²³⁵ Para 9 of the C-176/03 judgement

²³⁶ Communication from the Commission to the European Parliament and the Council on the implications of the Court's judgment of 13 September 2005 (Case C 176/03 Commission v Council) COM/2005/0583 final/loc. cit. 125 p. 4-5

*ceeds of crime*²³⁷.

So, although the EC had no competence to demand the Member States to criminalise money laundering in the beginning of the 1990's, now in the 21st century the EC has competence to do that. So, at least the questions relating to criminal law competence have not watered down the EU's AMLS. But has the flexibility of the terms of the AMLS done that?

7.1.2 Flexibility of the AMLS – the Problem of the Non-uniform Implementation

There have also been lots of criticism that EU's new risk-based approach results too flexible definition of *actus reus* of money laundering crime. The broad character of the AMLS can, however, regarded to be necessary in order to be able to respond the ever-changing nature of the phenomenon, the Chameleon threat. On the other hand, too flexible terms may fail to provide clear guidance and to lead to inconsistencies, this all can be seen to have a potential risk to lead to violation against *nullum crimen sine lege* principle, and thus questions about both legality and foreseeability can arise²³⁸.

The idea behind the AMLS accommodating flexible definitions seems to be benevolent – every country makes that kind of legislation as it needs. But in reality every country has its own views and they may not feel that they would need any kind of extra measures in addition to the obligatory ones. But how has this flexibility of the EU's AMLS affected in practice?

Due to lack of space in this piece of written work there will only be analysed the implementation of the main points of the EU's AMLS in Finland and in the UK. In Finland there is no offence of conspiracy available for the basic offence of money laundering. When considering the CDD -principles, there are no requirements to identify the beneficial owners of legal persons and no requirement to conduct ongoing CDD on the business relationship. Some CDD exemptions are also in place in the banking and insurance sectors and there are no CDD requirements with respect to PEPs. Also limited provisions are in place with respect to the risks associated with non-face to face business relationships and transactions. Casinos are subject only to the general requirements with no additional requirements or binding standards in place to govern their conduct regarding AML issues. Finland does not eit-

²³⁷ Communication from the Commission to the European Parliament and the Council on the implications of the Court's judgment of 13 September 2005 (Case C 176/03 Commission v Council) COM/2005/0583 final

²³⁸ G Stessens, *Money Laundering. A New International Law Enforcement Model* (Cambridge University Press, Cambridge 2000) 127

her have a national mechanism to consider requests for freezing from other countries or to freeze the funds of EU internals.

When considering the UK, there does not exist any enforceable obligation regarding to PEPs²³⁹. The other thing which is not fully taken into legislation in the UK are the CDD -principles. In the UK the guidance only partly deals with identification where there are doubts regarding previously obtained customer identification data. It is not either specifically required by law or regulation to verify that any person purporting to act on behalf of the customer is so authorised. Also there is no requirement in law to identify the beneficial owner. There is neither explicit obligation to obtain information on the purpose and nature of the business relationship in the UK in all cases. A requirement to conduct ongoing monitoring does not exist in law and provisions for reduced/simplified CDD are overly broad.

There seems to exist similar tendency also in Portugal and in Sweden that they do neither have enforceable obligation regarding to PEPs and also they are not fully compliant to the CDD -principles²⁴⁰. So, it can be concluded from above that the EU's target to have a similar AML legislation in every Member State has failed at least at this point. And as a result of this the European Commission has decided to pursue infringement procedures against 15 Member States for failure to implement the Third Anti-Money Laundering Directive in national law.²⁴¹

7.1.3 Pluralisation/Responsibilisation strategy – Works Well in Theory But Not so Well in Practice

The aim of the pluralisation/responsibilisation strategy²⁴² is that the institu-

²³⁹ FATF. Summary of the third mutual evaluation report anti-money laundering and combating the financing of terrorism. United Kingdom and Ireland.

<<http://www.fatf-gafi.org/dataoecd/33/20/38917272.pdf>> (accessed 2.11.2008)

²⁴⁰ FATF. Summary of the third mutual evaluation report anti-money laundering and combating the financing of terrorism. United Kingdom and Ireland.

<<http://www.fatf-gafi.org/dataoecd/33/20/38917272.pdf>> (accessed 2.11.2008)

and FATF. Third mutual evaluation report anti-money laundering and combating the financing of terrorism. Sweden. <<http://www.fatf-gafi.org/dataoecd/26/35/36461995.pdf>> (accessed 2.11.2008)

²⁴¹ Rapid- press release. Anti-money laundering: Commission takes measures against 15 Member States for non timely implementation. (5.6.2008)

<<http://europa.eu/rapid/pressReleasesAction.do?reference=IP/08/860&format=HTML&agend=0&language=EN&guiLanguage=en>> (accessed 4.11.2008)

²⁴² The phenomenon which Levi calls 'new policing'. M Levi, 'Evaluating the 'New Policing': Attacking the Money Trail of Organised Crime' (1997) 30 Australian and New Zealand Journal of Criminology 1

tions and persons covered by the Directives become active parties, pro-active agents, in fight against money laundering. And as a result of this they have a heavy duty to co-operate with authorities and also to adopt what Mitsilegas calls a *predominant climate of suspicion*²⁴³. This moral crusade towards financial institutions has eroded professional secrecy and also undermined the right to privacy – and there has already been rising numbers of arguments about balancing the need for requiring information for security reasons versus individual privacy rights²⁴⁴. The question can also be cast whether in any case the outcome of this jigsaw puzzle, like the self-regulation of financial institutions, can be legal certainty.

The EU's AMLS has combined both transaction size based and suspicion based systems thus creating a hybrid system.²⁴⁵ The threshold based system, the objective one, was regarded too expensive and increasing institutions workload too much. The suspicion based model is more cost-effective although it needs well educated staff and is totally subjective²⁴⁶ and can be more unreliable and more vulnerable to corruption. Thus by combining the both systems the EU has tried to diminish the costs and the work load of actors covered by the Directives but also avoided to establish subjective system, based at least partially on the culture related gut feeling.

But the pluralisation/responsibilisation strategy is not problem-free e.g. '*myth of amoral business*'²⁴⁷ can undermine this strategy. Not to mention that some professionals like lawyers will also face additional work to find out who the beneficial ownerships and in some countries it is not even possible (even for the banks!)²⁴⁸. Mitsilegas²⁴⁹ also argues that EU tries with its AMLS to activate non-state actors to fight against money laundering because the criminal justice system does not have enough resources to fight alone. He sees this strategy vulnerable because individuals who lack the law enforcement knowledge are forced to police the society.

²⁴³ V Mitsilegas, *Money Laundering Counter-Measures in European Union: a new paradigm of security governance versus fundamental legal principles* (Kluwer Law International, The Hague 2003)

²⁴⁴ 'Money Laundering' (An article on the website EurActiv.com 27.5.2005) <<http://www.euractiv.com/en/financial-services/money-laundering/article-139944>> (accessed 2.8.2008)

²⁴⁵ H Ping, '*The Suspicious Transactions Reporting System*' (2005) 8 J.M.L.C. 254

²⁴⁶ H Ping, '*The Suspicious Transactions Reporting System*' (2005) 8 J.M.L.C. 254

²⁴⁷ Ibid

²⁴⁸ T Buck, '*New money laundering laws put more onus on professions*' Financial Times (Brussels 27.5.2005) <<http://www.ft.com/cms/s/4457bf4e-ce4d-11d9-9a8a-00000e2511c8.html>> (accessed 29.8.2008)

²⁴⁹ V Mitsilegas, *Money Laundering Counter-Measures in European Union: a new paradigm of security governance versus fundamental legal principles* (Kluwer Law International, The Hague 2003)

The financial and the non-financial institutions which have not been delighted about the extra work and costs of regulation imposed to them. The EU's AMLS is not either been received with verve by the professionals like bankers and lawyers. It is also claimed that lawyers are put in 'impossible moral situation' when they are trying to carry on their relationship with clients without committing a tipping-off offence²⁵⁰.

As noted above some of the methods introduced in the EU's AMLS have been more successful than others. However, the strategy could be improved regarding the flexibility of the terms and also regarding the pluralisation/responsibilisation strategy. The main deficit, the competence regarding the criminal law matters, has been solved already so that is a good foundation stone on which the EU can build a comprehensive AMLS. But has this AMLS achieved a significant reduce in the amounts of money laundered or have it have deterrence effect on the OC in the EU soil? This will be discussed next.

²⁵⁰ R Rothwell, 'UK firms suffer as reporting rules bite' (2007) L.S.G

8 THE STORY OF SUCCESS OR THE STORY OF THE TEARS?

The answer to the question posed in the title is: No one really knows. It seems that the EU has put a lot of effort and money to establish its AMLS but has totally forgotten to establish any proper means, how to assess its impacts. So, it seems that the major deficit in the whole EU AMLS is the total absence of the tools using which the success of the strategy could be evaluated. The good news however is that finally in 2007 the Commission noticed this and established a working group, *the Eurostat Working Group* to assist with the collection of statistical data on money laundering and to set up a *Task Force* to examine the results. The work of this Eurostat Working Group is currently going on – at the time of writing this thesis, the Working Group has issued a Document²⁵¹ in which it introduces some tools which could be used to assess the effectiveness of the strategy. These tools include number of different indicators using which a total picture of the amount of money laundering in the each Member State could be assessed and then the amount of money laundering at the EU level could be calculated. These indicators include e.g. number of STRs, number of cash smuggling operations detected and amounts frozen/confiscated. The development of that kind of evaluation system is not an easy one because of the lack of statistics in some Member States. According to this Document of the Eurostat Working Group, the aim is to collect information from Member States relating to three stages; reporting/intelligence –stage, investigation –stage and judicial –stage. In the Document it turns out that for example only five Member States are able to provide data on number of requests received for freezing orders from another Member State. The document contains similar question relating the ability of Member States to provide data and it seems that there is so much work to do before there can be even a dream of the EU-wide statistics relating to money laundering.

So, if some sort of assessment of the effectiveness of the EU's AMLS is wanted to made right now, it can only be by using the information obtained from different sources like from the FATF or Europol. The information is based on the country reports issued by the country itself. That is why the current assessment of the effectiveness is complicated and there cannot be drawn a clear and reliable picture how well this AMLS has achieved its aim. And when the above mentioned tool of assessment is ready there cannot any more be obtained information about the amount of the money laundered before Directives/FWDs/Joint Actions or the impact of for example the Amen-

²⁵¹ European Commission. Money-laundering – Data Availability. Document ESTAT/CR/TF2008/3

ding Directive, so the amount of money laundering before AMLS remains in darkness.

However, although the absence of any formal EU-wide indicators relating to the money laundering I want to bring some sort of information to this piece of research about the effectiveness of the AMLS. The lack of the space limits the review to very small one. If the STRs are regarded to be good tool for assessing effectiveness, the following tells about the effectiveness of the strategy. In the UK the total number of STRs submitted in 2005 was just under 195,000 compared with less than 20,000 in 2000 and less than 100,000 in 2003. The most prolific reporters were banks (65% of the total) and accountants (7.5%), the year 2005 saw a significant growth in reporting from bureaux de change, and insurance and finance companies²⁵². In Finland the trend has been similar; in 2000 there were 1,109 reports, 2005 the amount of STRs was 3,495 and in 2007 already 17,370²⁵³. If the amounts of frozen or confiscated assets relating to money laundering are considered better tools of assessment, the following trends can be found. The amount of the assets frozen relating to money laundering in Finland 2003-2007 grew from 750,000 euros to 820,000, being in year 2006 even 23,500,000 euros. In the UK the amount confiscated grew from £38.8m in 2003/04 to £96.3m in 2007/08²⁵⁴. However, it is not known whether these numbers mirror the more efficient legislation or just whether the amount of money laundered and the money laundering attempts have grown because of for example the four freedoms in the EU area. These means of assessment are not any way perfect but they can be considered to give some sort of information at least the eagerness of the financial institutions and other actors to provide information about suspicious transactions.

So, due to the lack of any proper tools for assessment, the effectiveness of the EU's AMLS seems to remain unknown. The AMLS lacks one vital part – the tool which could be used to assess the strategy. But luckily the EU is now trying to find a proper tool for it – but a word of warning; it won't be an easy task!

²⁵² S Landen, Review of the Suspicious Activity Reports Regime.

<http://209.85.135.104/search?q=cache:EW_MUrZTfYkJ:www.soca.gov.uk/downloads/SOCAtheSARsReview_FINAL_Web.pdf+suspicious+activity+reports+statistics&hl=fi&ct=clnk&cd=7&client=firefox-a> (accessed 5.11.2008)

²⁵³ KRP. Rahanpesun selvittelykeskuksen puolivuotiskatsaus 2008.

<[http://www.poliisi.fi/poliisi/krp/home.nsf/files/RAP_puolivuotiskatsaus%202008/\\$file/RAP_puolivuotiskatsaus%202008.pdf](http://www.poliisi.fi/poliisi/krp/home.nsf/files/RAP_puolivuotiskatsaus%202008/$file/RAP_puolivuotiskatsaus%202008.pdf)> (accessed 1.11.2008)

²⁵⁴ European Commission. Money-laundering – Data Availability. Document ESTAT/CR/TF2008/3

9 CONCLUSION

'The trick of regulation is to minimise the illegitimate exploitation without wrecking the economic dynamism'²⁵⁵.

The global fight against money laundering initiated by the Vienna Convention in 1988 has gone through various different phases and different global and regional actors, like the FATF, the Council of Europe not to mention the EU, have taken part to it. This all has resulted a wide global network of AML actors, building a collaborative preventive approach. To these actors it has been clear that in the absence of an effective international co-operation, there would be no realistic chance of curbing money laundering.

The rationales behind this global AML crusade have been manifold and partly controversial – arguments being cast both for and against the criminalisation of the money laundering. The efforts to tackle organised crime and the fight against drugs as well as the aim to protect financial institutions and to prevent terrorism related money laundering to take place have branded the anti-money laundering efforts in the different decades. Some theories of legitimisation of money laundering has also been cast but without any significant success.

The *'dark figure'* of the money laundered and the complexity of the money laundering phenomenon have not made the efforts to regulate money laundering a piece of cake. The Three Stage -model with its three stage approach has also lead to wrong direction because of its tendency to see money laundering consisting of three different phases which take place in the same order in every money laundering case. Luckily there now seems to be a step towards more flexible approach of money laundering phenomenon, to Chameleon theory. This theory sees money laundering more as a process in which the three stages can be in different order or some of them can be absent and it thus reflects the complexity of money laundering.

The EU's AMLS is a quite new-born – only about two decades long effort which has aimed to regulate money laundering. The EU has seen the money laundering being among the fifteen areas of EC's particular interest because of its close relationship with core EC interests, cross-border importance and political importance. The EU's AMLS is an important tool in the fight against OC and in the protection of EU's financial interests, and the integrity of the internal market, especially the four freedoms and the Single Payment Area. But the things are not so easy as they may seem to be be-

²⁵⁵ M Levi, 'Money laundering: Risks and Counter-Measures' in A Graycar and P Grabosky (eds) *Money Laundering in the 21st Century: Risks and Countermeasures* (Canberra: Australian Institute of Criminology 1996) 3

cause the EU has had to balance between the free movement of capital and payments and the effective regulation of the money laundering. The strong political pressure from the US and other global AML actors has also been a motor for the EU to introduce its own AMLS.

The EU's AMLS has consisted of variety of legal tools like FWDs, three AML Directives, regulations and Joint Actions, being thus a double-text approach and been mainly built by taking account previous global anti-money laundering efforts, for example 40+9 Recommendations by the FATF, the UN tools and the work of other global and regional actors. The EU has not had to be very inventive regarding the contents of its legislative tools but it has been largely copy-cattng the other actors. Some of the efforts by the EU/EC have been made without proper legislative base and have thus not been even legally binding, like the demand for criminalise money laundering in the first Directive, whereas some parts of the instruments have been largely ad hoc, like the terrorism related part in the third Directive.

The main stumbling blocks in the EU's AMLS have been the questions relating the lack of competence in criminal law matters, e.g. the ability to impose criminal law sanctions and to criminalise certain acts, the heavy burden imposed on the financial institutions by the pluralisation/responsibilisation strategy, the imperfect understanding of the money laundering phenomenon and the flexibility of the AMLS. The main deficit of the strategy is, however, the total absence of any tools which could be used to assess the effectiveness of the strategy.

As seen in the EU's AML crusade, the EU has systematically developed its activities in the field of penal law and it has become a major actor in the formulation of the control policy, the latest stage of the development being the judgement of the ECJ that allowed the inclusion of provisions of substantive criminal law to Community legislation if this is necessary for the attainment of the objectives of the Community²⁵⁶.

The main challenge for the EU's AMLS is to provide an effective legal weapon to fight against money laundering. This weapon should be proportionate and not to impose too heavy burden on the law-abiding actors in society. Also one of the crucial things is the ability of the EU to be able to regularly update its AMLS in the light of developments and experience. The point is that if regulations need to exist, they need to be proportionate to the risk and focused on the major risks and recognise the costs to different parties any benefits derived. The real test is to find a regulatory approach that is not too burdensome but which is proportionate to the risk.

²⁵⁶ C-176/03 Commission of the European Communities v Council of the European Union [2005] OJ C 315, 10.12.2005

Abstract

The global fight against money laundering initiated by the Vienna Convention in 1988 has gone through various different phases and different global and regional actors, like the FATF, the Council of Europe not to mention the European Union (EU), have taken part to it. To these actors it has been clear that in the absence of effective international co-operation, there would be no realistic chance of curbing money laundering.

The rationales behind this global anti-money laundering (AML) crusade have been manifold and partly controversial – arguments being cast both for and against the criminalisation of the laundering. The ‘dark figure’ of the money laundered and the complexity of the money laundering phenomenon have not made the efforts to regulate money laundering a piece of cake. The Three Stage -model with its three stage approach has also lead to wrong direction but luckily there now seems to be a step towards more flexible approach of the money laundering phenomenon, to Chameleon theory of money laundering.

The EU’s anti-money laundering strategy (AMLS) is a quite new-born – only about two decades long effort which has aimed to regulate money laundering. The EU has regarded the dangers arising from organised crime (OC) being such that the Union should take some steps to minimise those dangers for its markets. Money laundering is regarded as an inherent part of OC activities and thus the EU has been eager to address the problem. The EU has seen the money laundering being among the fifteen areas of EC’s particular interest because of its close relationship with core EC interests, cross-border importance and political importance.

The EU’s AMLS has consisted of variety of legal tools like framework decisions, three AML Directives, regulations and Joint Actions, being thus a double-text approach and been mainly built by taking account previous global anti-money laundering efforts, for example 40+9 Recommendations by the FATF, the United Nation’s tools and the work of other global and regional actors. The EU has not had to be very inventive regarding the contents of its legislative tools but has been largely copy-cattng the other actors. Some of the efforts by the EU/EC have been made without proper legislative base and have thus not been even legally binding, like the demand for criminalise money laundering in the first Directive (91/308/EEC), whereas some parts of the instruments have been largely ad hoc.

The main stumbling blocks in the EU’s AMLS have been the questions relating the lack of competence in criminal law matters and the total absence of any tools which could be used to assess the effectiveness of the strategy.

But there still remains a question to what extent the EU's AMLS is actually effective or is it at all. It is clear that the AMLS has not been able to interfere with some key elements of money laundering like the underground banking system, tax havens or sufficiently to detect the cross border flows of monies. But at least now the money laundering is a specific criminal offence throughout the Union, whereas this was the case in only one Member State when the Commission proposed the Directive in March 1990.

Tiivistelmä

Vielä muutama vuosikymmen sitten rahanpesua ei nähty ongelmallisena. Huomionarvoista on kuitenkin se, että kahden viimeisen vuosikymmenen aikana tapahtunut valtaisa kehitys rahanpesunvastaisissa toimissa. Rahanpesunvastaisen sodan alullepanijana voidaan nähdä vuoden 1988 Wienin sopimus. Tätä sopimusta on seurannut lukuisat alueelliset sopimukset ja monet organisaatiot, muun muassa FATF, Euroopan Neuvosto ja YK, ovat olleet aktiivisia uuden rahanpesunvastaisen politiikan luomisessa. Euroopan Unionin rooli on kuitenkin ollut rahanpesunvastaisissa toimissa erityisen merkittävä jo senkin vuoksi, että EU:lla on huomattavasti valtaa jäsenmailhinsa (*sui generis*). Rahanpesunvastainen taistelu, rahanpesun rajoja ylittävän luonteensa vuoksi, vaatii erityisesti globaalia yhteistyötä ja tästä syystä onkin erityisen tärkeää, että alueelliset ja globaalit toimijat ovat olleet aktiivisesti mukana rahanpesunvastaisessa taistelussa.

Rahanpesunvastainen taistelu on kuitenkin ollut kaikkea muuta kuin helppoa. Rahapesu on erittäin monimutkainen prosessi ja tekniikan kehittyminen luo koko ajan uusia keinoja pestä rahaa. Erityisesti se, että menneinä vuosina on pidetty kiinni visusti ns. kolmen portaan mallista rahanpesun kuvaajana, on joiltain osin jopa johtanut siihen, että ei ole kyetty havainnoimaan kaikkein hienostuneimpia rahanpesun menetelmiä. Esitänkin tässä työssäni, että ns. kameleontti -mallin tulisi korvata, jopa jo kirveenkirjoitettuna pidetty ja aikoja sitten jo vanhentunut, kolmen portaan malli.

Rahanpesun laajuudesta ei myöskään voida esittää mitään varmoja tietoja, arviot sen laajuudesta vaihtelevat hurjasti. Kritisoiematta ei ole myöskään jäänyt rahanpesun näkeminen pelkästään haitalliseksi ilmiöksi vaan kirjallisuudessa esitetään myös näkökantoja siihen, että rahanpesu ei olisi välttämättä ollenkaan haitallista. Toisaalta taas suurin osa asiantuntijoista on sitä mieltä, että rahanpesu on erittäin haitallista sekä maailmantaloudelle että yksittäisille kansantalouksille, koska se ruokkii erityisesti järjestäytyneitä rikollisuutta.

Euroopan Unioni alkoi rahanpesun vastaisen taistelunsa 1990-luvun alussa. EU lähti kitkemään rahanpesua, koska se halusi vaikeuttaa järjestäytyneen rikollisuuden toimintaa alueellaan. EU:n rahanpesunvastainen strategia koostuu useista eri lainsäädännöllisistä instrumenteista kuten direktiiveistä, puittepäätöksistä, säädöksistä ja yhteistoimista. Tärkeimpänä näistä on kuitenkin kolme rahanpesunvastaista direktiiviä. EU on kuitenkin kopioinut suurilta osilta rahanpesunvastaisen strategiansa muilta rahanpesunvastaisilta toimijoilta kuten FATF:lta ja YK:lta ja ollut itse täten vähemmän innovatiivinen.

EU:n rahanpesunvastainen taistelu ei ole kuitenkaan sujunut ongelmitta. Ensinnäkin tämä taistelu on herättänyt kysymyksiä EU:n kompetenssista vaatia jäsenmaitaan kriminalisoimaan ja sanktioimaan tietyt teot. Toiseksi ongelmia on tuottanut EU:n 27:n eri jäsenmaan erilaiset intressit ja erilaiset oikeusjärjestelmät sekä se, että traditionaalisesti rikoslaki on katsottu heijastavan jokaisen kansallisvaltion suvereenisuutta. Yhtään helpommaksi näitä EU:n rahanpesunvastaisia toimenpiteitä ei ole tehnyt se, että EY-tuomioistuin on ollut aktiivisesti mukana määrittämässä EY:n rikosoikeudellisen toimivallan laajuutta. Itse asiassa tuomioistuimen päätökset ovat sekoittaneet pakkaa vielä entisestään.

Suurimpana ongelmana Euroopan Unionin rahanpesunvastaisessa strategiassa on kuitenkin ollut se, että se ei ole kehittänyt mitään mittareita joiden avulla rahanpesun vastaisten toimenpiteiden onnistuneisuutta voisi arvioida. Tällä hetkellä ei ole olemassa mitään luotettavia arvioita siitä, millainen vaikutus rahanpesun määrään tällä EU:n rahanpesunvastaisella strategialla on ollut.

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