

The regime that FATF built: an introduction to the Financial Action Task Force

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Abstract This article serves to introduce this special issue of *Crime, Law, & Social Change* on the Financial Action Task Force (FATF). It provides a primer on the history and purpose of FATF and lays out some of the central debates over FATF and the anti-money laundering (AML) regime. Finally, as a way of giving readers an overview of the articles in the special issue, it proposes a series of themes that academics and practitioners should consider in future research and work with FATF.

Introduction

In April 2016, the murky world of illicit finance burst onto the headlines of media outlets around the globe when the International Consortium of Investigative Journalists (ICIJ) published the now famous “Panama Papers.” The massive project, led by Bastian Obermayer and Frederik Obermaier of *Süddeutsche Zeitung*, was based on information leaked by someone working “on the inside” at Mossack Fonseca, a global law firm based in Panama. Nearly 400 journalists from over 70 countries pored over 11.5 million documents detailing 40 years of financial dealings. As the ICIJ describes them, the documents allow “a never-before-seen view inside the offshore world—providing a day-to-day, decade-by-decade look at how dark money flows through the global financial system, breeding crime and stripping national treasuries of tax revenues.”¹ The data directly implicated current and past heads of state in ten different countries. Many others had close family members who were named, a major red-flag in illicit

¹<https://panamapapers.icij.org/blog/20160403-new-icij-investigation-exposes-rogue-offshore-industry.html>. Among many other distinctions, the Panama Papers investigation won a Pulitzer Prize for its work.

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finance. The prime minister of Iceland stepped down within days of the project's publication. Especially when combined with recent high-profile cases of money laundering involving major international banks (PNB Paribas, HSBC, JPMorgan Chase, and Deutsche Bank), the Panama Papers convey a sense that illicit finance is a wildfire on the plains of international finance: spreading ever faster, threatening to char the entire landscape.

Less commonly trumpeted in the headlines is a trend that might seem contradictory to headlines about the Panama Papers. Over the past three decades, the international community has built a far-reaching global governance regime that takes aim at illicit finance. At the center of this effort is the Financial Action Task Force (FATF).² While FATF is relatively unknown to people who do not work directly with it or study it, FATF and the anti-money laundering (AML) rules it promulgates have become primary tools of economic and security policy, both foreign and domestic. Indicating its significance, G20 leaders in the wake of the 2008 global financial crisis included FATF as a vital player in efforts to build "a new international financial regulatory architecture" alongside other financial celebrities like the IMF and the OECD.

Why do we see a seeming increase in illicit money alongside an increasingly prominent global governance regime to fight it? Experts disagree. Detractors portray FATF as a faceless, unaccountable, *de facto* global regulatory agency run amok. On behalf of the interests of a few select states, it imposes regulations that are illegitimate and costly. For these critics, the Panama Papers are evidence that the rules are ineffective, to boot.

Apologists argue that the increase in money laundering cases is exactly what we should expect to see as the global AML regime strengthens. We might not be seeing more money laundering, but, rather, more money launderers being caught. Supporters emphasize that FATF's standards must pass through domestic regulatory systems before they take effect and that the private sector has an increasing say in forming the standards. The costs and benefits of FATF and AML, they argue, must be measured against the costs of the illicit activity it targets.

The articles gathered in this special issue aim to shed light on debates over FATF and the AML regime. Regardless of whether FATF's net impact is positive or negative, it is indisputable that the fight against illicit money has bled into nearly every corner of government activity. In foreign policy, tracking and freezing assets of enemies has become a common, even primary, tool.³ "Following the money" is perhaps the most important tool in fighting transnational crimes ranging from illicit narcotics to nuclear proliferation to terrorism. AML also affects economic development. Effective AML systems can promote development by preventing corruption or boosting government revenue. AML regulations can also hinder development. To avoid AML-based fines, for example, banks in recent years have been pulling out of under-developed regions because customer verification is more difficult—a move known as "de-risking." This leaves the poor with diminished access to credit and other financial services. These economies become more dependent on cash, which is a boon for the black market and for the crime and corruption it sometimes supports. Finally, AML has become a significant cost for any entity that deals with financial services. Banks, law firms, and non-profit organizations

² Originally known as the Financial Action Task Force on Money Laundering.

³ For the most vivid example, see Zarate [1].

spend billions on AML every year. Compliance has become a bona fide profession, with organizations, professional standards, and journals. Multiple universities now offer certificates or advanced degrees designed specifically for people seeking careers in compliance. In short, in nearly any field or profession, anti-money laundering and the effort to fight illicit finance have grown to be important factors.

Despite its importance, the multi-level regime that aims to tackle illicit finance remains understudied. By describing, analyzing, and critiquing FATF and the regime it has built, this special issue aims to address that gap while inspiring other scholars to shed their own light on it. Illicit political economy, in particular, requires a multi-disciplinary approach because it lies at the intersection of the social sciences [2]. The articles in this special issue come from scholars in criminology, political science, economics, law, sociology, and public policy. This multidisciplinary approach also avoids presenting a single narrative on FATF and the AML regime. Instead, it shows the regime's widespread relevance to a variety of fields. It also presents those interested in thinking about it with a range of questions and answers to consider.

This introduction aims to be a primer for those less familiar with FATF, to facilitate reading the articles that follow, and to underscore prominent themes that are relevant to the real-world operation of FATF. I leave specific debates within scholarship on FATF and AML to the authors to cover as necessary. In the following section, I draw on secondary literature to discuss why many experts consider money laundering to be an important, and difficult, problem to tackle. The third section provides a finer-grained look at the evolution of decision-making within FATF. This draws on several years of elite interviews in multiple countries. The fourth section provides readers with an overview of the articles to follow. It does so by highlighting key questions that the articles included in this issue suggest are relevant for on-going conversations about the future of FATF and the governance of illicit finance.

Understanding the challenge

Money laundering lies at the nexus of the licit and illicit economies and intertwines the two in dangerous ways [3, 4]. Simply defined, money laundering is any attempt to hide the illegal sources of profit. The story of the Bank of Credit and Commerce International (BCCI) is perhaps extreme, but illustrative of the state of play when FATF began. Regulators around the globe seized BCCI's assets in 1991, in what Potts et al. [5] describe as "a scandal of nearly unimaginable proportions....". The client list of the bank was impressive. Truell and Gurwin [6] write:

...BCCI had outwardly seemed like a normal financial institution, with attractively designed branch offices, its own traveler's check business, and a reputation for financing international trade. But behind this convincing façade, BCCI was a criminal enterprise that catered to some of the most notorious villains of the late twentieth century, including Saddam Hussein; leaders of the Medellín cartel, which controls the bulk of the world's cocaine trade; Khun Sa, the warlord who dominates heroin trafficking in Asia's Golden Triangle; Abu Nidal, the head of one of the world's leading terrorist organizations; and Manuel Antonio Noriega, the drug-dealing former dictator of Panama."

Showing how complex the world of money laundering can be, the bank also had close ties to then-president George H.W. Bush and his successor, Bill Clinton (see also [5, 7]; for similar histories tying crime to money laundering, see [7, 8]). Potts et al. [5] report that BCCI was key to the Central Intelligence Agency's activity in the Iran-Contra affair. At the heart of this network was a thriving money laundering business.

Some say the term "money laundering" stems from early twentieth century criminals' use of laundromats to hide their money. While that story may be apocryphal, as a metaphor it illustrates the difficulties in fighting money laundering. A cash-based laundromat provides no paper trail of the number of people who use it. As a result, it would be easy for would-be money launderers to take money earned illegally, say from a drug smuggling ring, and place it "on the books" at a laundromat by claiming that more people had used the facility than actually had. To beat that system, the authorities would have to surveil the locale, count the customers and the loads of laundry, and compare their own numbers to those provided by the facility's owners. If the launderer owned a string of laundromats, oversight quickly would become quickly becomes very expensive. Imagine now a string of laundromats, all owned under different names and in different legal jurisdictions. Casinos, banks, and other deposit-taking institutions that fail to verify account owners' true identities—the "beneficial owners"—can do the same. They render the source of money almost impossible to find.

Today's fast-moving, increasingly global financial system could have the same effect, because money moves faster than those tracking it. That is why a small state with a relatively undeveloped financial system can pose a significant challenge to those seeking to oversee the financial system. Such was the case in 2000, for example, when tiny Seychelles passed its Economic Development Act, guaranteeing immunity from foreign asset seizure to anyone investing over US\$10 million in the nation's struggling economy. Even assuming that those seeking to stop the flows of such funds have aligning preferences and know what the correct solution to the problem is, effectively implementing a regime in such a porous context is challenging. If we relax the highly stylized assumptions of aligned preferences and knowledge of the "correct" solution, as the Panama Papers story suggests we should, the challenge grows significantly.

Of course, if money laundering is simply the act of hiding, or attempting to hide, illegal sources of profit, one might reasonably ask whether this is such a tremendous problem. In many ways, it seems like the "little white lie" of international crime: perhaps it is not good, but neither is it heinous. R.T. Naylor [9] makes this argument most directly, writing that "money laundering is an artificial and contrived offense that has no place in the statute books of a civilized country."

In general, however, Naylor's voice seems to be in the minority, even among skeptics of the current system. That is because money laundering poses a variety of significant problems. Guy Stessens [4], for example, argues that money laundering can generate financial instability and erode public confidence in the banking system. It employs labor and capital in inefficient, socially disruptive activity and leads to a suboptimal investment of capital. Laundered money is often used to pay off politicians and regulators, and so contributes to corruption. Laundered funds can be used to expand or maintain the illegal activity from which they came, or to diversify a criminal organizations portfolio, making them more resilient [3]. Ultimately, money laundering is a necessary, although not sufficient, aspect of much crime to begin with. The primary

logic behind most AML policies is preventive: reduce the profit, reduce the crime. Regulators thus see money laundering not as the little white lie of international crime, but as the tip of the iceberg.

Trying to control that iceberg requires substantial international cooperation, for a number of reasons. The most obvious reason is the integration of the financial sector. Advances in information technology allow investors to send money around the world quickly, cheaply, and easily [10]. This might be in search the best return on a legitimate investment; it also might be in search of jurisdictions that allow money laundering. Either way, the mechanisms of finance are faster than the mechanisms of policing. In the time that it takes local law enforcement to secure permission to act, launderers can send funds through a maze of jurisdictions, moving evidence beyond law enforcement's reach. This issue of speed is exacerbated by innovations specifically designed to avoid oversight; "walking trust accounts" automatically send funds to a new jurisdiction if an inquiry is ever made on the account [11]. Thus, states need to cooperate in order to clamp down on all links of the criminal chain. For this reason, much of the negotiations surrounding any AML agreement focus on the ability of police and judicial actors to cooperate across borders.

This demand for cooperation only intensifies when attempting to track money designed to fund terrorism, which has been a central goal of FATF since 2001 [12, 13]. Flexible and informal networks of terrorists can adapt relatively easily if caught. In addition, many terrorist operations require relatively small amounts of money. In a system designed to track the millions, or even billions, of dollars involved in drug-trafficking, transactions in the tens of thousands or even below easily fall below the radar. This is still more true if funding is passed hand to hand among trusted network members, as is done in *hwala* systems. As with the mainstream financial system, most transactions sent through *hwala* financial systems are perfectly legitimate transactions. The challenge is to separate the desirable from the undesirable without quashing the market entirely. This linking of AML to security politics also raises the degree of politicization around AML, especially given the contentious politics of the so-call "War on Terror."

The international fight against money laundering, then, is a microcosm of the fundamental challenge of global governance today, particularly as it pertains to illicit markets. A globalized financial system allows money, whether licit or illicit, to move around increasingly freely. Those seeking to regulate it, however, are bound by traditional conceptualizations of sovereignty and held back by the legal boundaries of their jurisdictions. The reach of existing governance institutions does not match the scale of the problems we face.

The evolution of governance as a response

AML before FATF

In 1980, the Council of Europe issued what seems to have been the first international agreement on money laundering. It promoted so-called "know-your-customer" principles in banking, the idea that banks should be responsible for ensuring that the name(s) on an account reflect the true beneficial owners of the funds. The agreement also called

on states to facilitate the tracking of banknotes across borders.⁴ However, it had little effect. States, seemingly unconcerned about money laundering, mostly ignored the statement. At the time, no states had criminalized money laundering.

Concern over money laundering grew in the late 1980s, as states grew more concerned with illicit narcotics trafficking. The United States, in 1986, became the first state to criminalize money laundering.⁵ A few other states, mostly within the G7, had legislation pending at the time, but these states remained the small minority. Nor did that group of states necessarily agree on the nature of the problem or the solution to it. Reflecting these divergent approaches, when the Basel Committee issued a statement on money laundering in 1988, it did not even provide a definition of money laundering.⁶

In 1988, the United Nations established the first international definition of money laundering in the Convention Against Illicit Traffic in Narcotic Drugs and Psychotropic Substances, or the Vienna Convention ([14]; [15]). As part of the fight against narcotics trafficking, the Convention obliged states to “deprive persons engaged in illicit traffic of the proceeds of their criminal activities and thereby eliminate their main incentive for so doing....”⁷ Again, however, states’ divergent preferences on the question severely weakened the Convention as an AML tool. The inclusion of money laundering was one of the most controversial points in an already controversial convention ([14]). The placement of AML within a counter-narcotics convention, however, reinforced the narrow framing of money laundering as a by-product only of the illicit drug trade.

By the end of the Vienna Convention negotiations, some state delegations doubted the wisdom of using UN Conventions to regulate money laundering. The convention took ten years to negotiate, making it an unlikely forum in which to regulate the highly adaptive world of finance ([14]–90). They argued that the process was too complex, the preferences too divergent, and the outcome too basic to be effective. (One interviewee active in the negotiations on behalf of the UN evaluated the process in explicit terms: “I would rather have my teeth pulled out than to sit through another one of those negotiations.”⁸) In response, the U.S. proposed establishing a one-year, fact-finding task force that would catalogue the AML statutes on the books around the world. Even that proposal met resistance for a year before all G7 members agreed to participate in the new Financial Action Task Force on Money Laundering [16].

The financial action task force takes shape

In the introduction to the first annual report, FATF members make it clear that concern over drug trafficking was the driving concern. They write: “The Heads of State or Government of seven major industrial nations and the President of the Commission of the European Communities... stated that the drug problem has reached devastating proportions, and stressed the urgent need for decisive actions, both on a national and

⁴ Recommendation No. R (80) 10 of the Committee of Ministers to Member States on Measures Against the Transfer and the Safekeeping of Funds of Criminal Origin. Adopted on June 27th, 1980.

⁵ US Money Laundering Control Act of 1986.

⁶ Council of Europe Recommendation No. R (80) 10, para. 2. “Statement of Principles on the Prevention of Criminal Use of the Banking System for the Purpose of Money-Laundering”

⁷ UN Vienna Convention.

⁸ Author interview.

international basis. Among other resolutions on drug issues, they convened a Financial Action Task Force (FATF)...." [17].

At its founding in 1989, then, FATF was an 11-member task force with a one-year mandate, focused solely on stopping the flow of funds from the illicit narcotics trade; estimating the amount of money laundered yearly entailed estimating the value of the narcotics market to the exclusion of all else [9, 18]. In the intervening decades, FATF members have broadened their focus to include transnational crime, terrorism financing, WMD proliferation, and, to a lesser degree, financial exclusion. Most recently, FATF members describe their efforts as ensuring the more generalized idea of "financial integrity." In its own words, FATF's objectives today are "to set standards and promote effective implementation of legal, regulatory and operational measures for combating money laundering, terrorist financing and other related threats to the integrity of the international financial system." There currently are 37 full members (including the European Commission), nine regional groupings as associate members, and 28 observer bodies.

Referring to FATF as an organization conjures images of a large international bureaucracy. In reality, FATF is better described as a transnational public policy network [19]. FATF's members, with the exclusion of the European Commission, represent a cross-section of states: large and small states, powerful and weak states, post-industrial and developing economies. State delegations often include a variety of domestic agencies, from Treasury officials to law enforcement. Observer organizations are a cross-section of global governance: from umbrella organizations like the IMF and World Bank to more specific organizations like the World Customs Union. FATF also brings in a wide range of people and institutions as part of the consultative network that surrounds its work, including representatives from private sector industries affected most directly by FATF's activities, including the bankers, lawyers, accountants, and non-profit organizations. FATF officials also participate regularly in other international fora as a means of diffusing its standards. Ultimately, FATF looks much more like a transnational, multi-level network than a quasi-hierarchical international organization.

The central norms of FATF are the "FATF 40 Recommendations." While the precision of the recommendations varies, they generally are broad and open-ended. States can and must write their own regulations that meet the goals set forth in the relevant recommendations. For example, Recommendation 9 (formerly Rec. 4) reads: "Countries should ensure that financial institution secrecy laws do not inhibit implementation of the FATF Recommendations." This is clearly a principle to guide legislation, not legislation that is to be adopted verbatim into domestic legislation.

Members informally review the recommendations annually. In cases in which a recommendation has proven unclear or difficult to implement, members often issue interpretative notes, which may be integrated into the official recommendations after a trial period. Members have fully and formally revised the recommendations three times, in 1996, 2003/4, and 2012 (see Nance, this volume).

There is no central agreement in FATF that outlines the decision-making procedures. Plenary meetings happen roughly 3 times a year. At least one of those meetings is in Paris, where FATF's small secretariat sits under the same roof as the OECD. Although this has led to some misperceptions that FATF is part of the OECD, FATF is an independent organization. Some of the staff, however, are seconded from the OECD. The secretariat is comprised of only 17 people, up from 12 when FATF was founded in

1989. The growth in staff relative to its responsibility is thus remarkably low. The secretariat has no vote and, until recently, performed an important, but largely organizational and facilitative role. Recently, FATF members decided that the secretariat would play a more active role in carrying out some of the core monitoring functions discussed below.

Meetings are run by the president, whom members elect by consensus. FATF presidents historically served one-year terms, but changes made in 2017 as part of an on-going reform process extended the term to two years. Members hold formal votes at the plenary, but those most often are symbolic. Decision-making is traditionally consensus-based. Agreements are hammered out before the plenary in working groups or in more social gatherings that surround the plenary meetings (including a somewhat infamous karaoke night that happens during most plenary gatherings).

FATF's monitoring powers are among the farthest reaching of any international organization. There are two key monitoring mechanisms. The most important mechanism is the mutual evaluation. Originally applied only to members, these invasive evaluations now apply on a rotating basis to all states that aim to comply with FATF standards. The evaluation entails an on-site visit by a team of experts. The monitoring team, comprised of other FATF members or representatives of international organizations, spends approximately one week interviewing relevant actors and making site visits. The team fills out a detailed, extensive "common methodology" that aims to gauge how the target state's AML system aligns with the 40 Recommendations. Members then discuss the results in a peer review in the Plenary. An unsatisfactory performance results in closer monitoring and the requirement to report again at the following Plenary on progress. While the evaluations originally were conducted by FATF staff and member representatives, the common methodology allows other international organizations, such as regional iterations of FATF or the World Bank, to conduct the evaluations. The peer review of that evaluation still happens at the FATF plenary among FATF members.

Second, "typology exercises" also play a monitoring role, although observers rarely acknowledge them as such. These exercises are both diagnostic and generative. The typology exercises bring together money laundering experts from around the world to discuss current issues in money laundering. They have three basic goals: to exchange information on any on-going cases and operations, to identify and describe current trends in money laundering, and to identify and describe effective (and failed) countermeasures. Since 1995, FATF has published the results of the exercises. The typologies have become more focused over time, with working groups established that are designed to intensify the scrutiny given to a particular topic.

Enforcement in FATF is a critical point of contention among scholars. There is a common belief that the FATF blacklists are a primary—even the primary—diffusion mechanism in the AML regime, although there is very little empirical evidence to show this. (For more details on this, see Nance (this volume), [20–24]). Enforcement in FATF has evolved over time. The current system—the International Cooperation Review Group—is a hybrid of previous blacklisting procedures and began in 2007. In 2009, the G20 called on FATF to strengthen the ICRG procedures and publicly name countries with deficient AML systems. The new procedure entails an initial mutual evaluation. If evaluation reveals a country's system to be insufficient, the ICRG reviews the report, with comments from the target jurisdiction. If the ICRG confirms the finding that a

country's system is too weak, FATF subjects it to more frequent monitoring. For the additional monitoring to end, the target must develop a comprehensive reform plan that is backed by a high-level political commitment. Seven countries are currently on that list: Bosnia and Herzegovina, Ethiopia, Iraq, Syria, Uganda, Vanuatu, and Yemen. The blacklist is comprised of states that have made no high-level political commitment to a reform plan. Only two countries have ever been on that list: North Korea (Democratic People's Republic of Korea) and Iran (Fig. 1).

Controversies and questions around FATF: key themes

With that primer on the basics of FATF in mind, the goal of this special issue is to reflect the most recent debates over FATF and the AML regime. The project also aims to gather insights from academic experts on FATF to help practitioners improve the AML system. That is not to say that the authors here necessarily agree on what “reform” of FATF should look like. For some, this might be increasing democratic participation, while for others it is emphasizing demonstrable progress against illicit money. This special issue as a whole, therefore, has no specific agenda beyond enhancing scholarly engagement with FATF and the AML regime, and enhancing the contribution of academic research to the operation of FATF.

In that regard, this special issue lands at an important time. In the 2016–7 plenary year, FATF delegates began a review of their formal mandate, including a discussion of governance within FATF. As always, members can choose to make this a relatively shallow exercise—one in which they make a few small institutional changes but effectively continue business as normal. Such an approach would betray FATF's strong history of innovation. We urge the members instead to take this moment to reflect more deeply, and more critically, on the tasks that remain and how best to address them. In that vein, the articles included in this special issue suggest five important themes that delegates should consider.

Common questions, different answers on FATF and AML

Question 1: What explains FATF's expansion and what does this mean about the future?

Looking back it is easy to assume that the current AML regime was a logical and likely outcome of FATF. Seen in historical context, however, the regime's expansion and FATF's evolution into a major financial actor today is unexpected. In 1998, Susan Strange [25] predicted that FATF was an empty effort by the G7 to be seen as doing something to respond to the expanding illicit narcotics trade in the 1980s. Thus, a primary theme—arguably *the* primary theme—of scholarship on FATF has been explaining the regime's expansion.

Scholars primarily argue that FATF is a tool that powerful countries—the EU Member States and/or the United States, in particular—use to force their preferences on other jurisdictions. Simmons [26, 27] argues that it reflects the preferences, soft and ill-formed, of the United States alone. Drezner [20] argues FATF's core agenda reflects

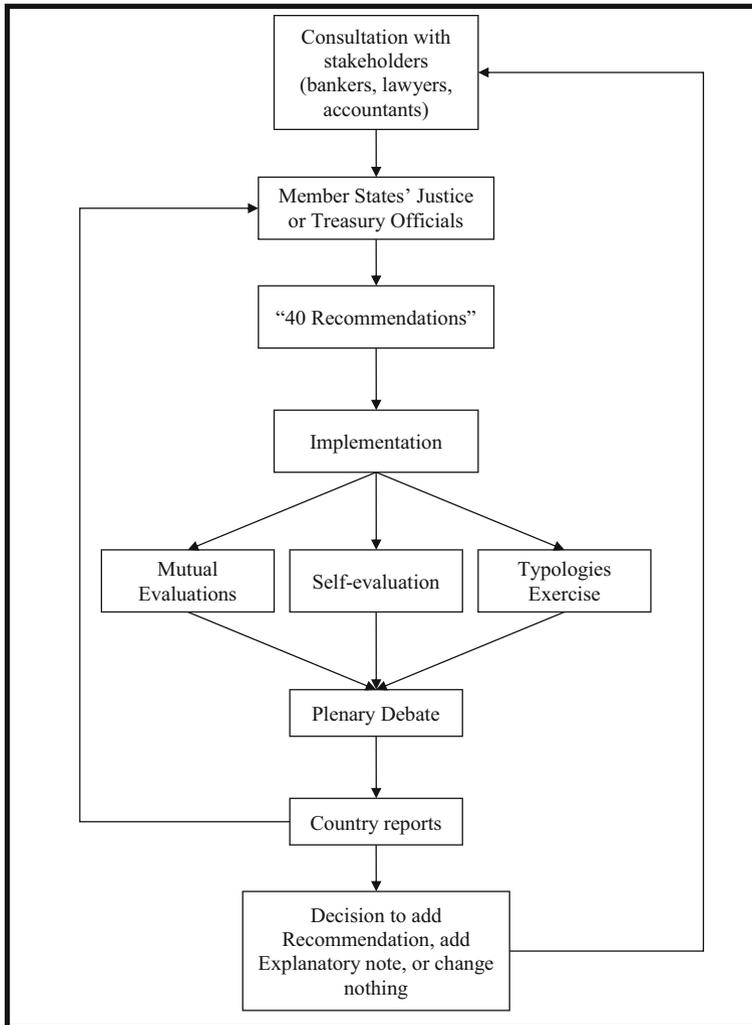


Fig. 1 A representation of the process by which participants have created and revised FATF standards

consensus among the US and EU member states, while the flexibility inherent in the recommendations reflect enduring disagreements on the details. From a more strategic constructivist angle, Sharman [23, 24] argues that the US and EU use FATF to paint non-compliant jurisdictions as rogue, unreliable players, thereby scaring off would-be investors. Jakobi [28] uses network analysis to map the influence of the United States.

Articles in this special issue move this debate forward, albeit in different ways. Inês Sophia De Oliveira suggests that we might be in a new phase of rule-making in FATF. She argues that while powerful states historically determined the regime's direction, today the private sector plays a much larger role, even challenging the primacy of the state. The private sector—in particular the financial services industry and its high-level representatives—is becoming a “non-great power influencer” in FATF. She writes that

the shift away from a rule-based system and toward a risk-based one is a strong and substantively important example of private sector influence and away from the state domination of earlier years. The changes are an evolution, however, not a paradigm shift.

My own contribution to this debate attempts to provide a novel interpretation of FATF. Emphasizing the evolution of FATF over time, I argue that FATF has been most influential when it has operated in line with the principles of “experimentalist governance” [29]. The ideal-typical experimentalist governance model emphasizes flexible and revisable standards over fixed and universal rules; broadly participatory networks over state centric quasi-hierarchy; and dynamic problem-solving over rule enforcement [30]. Social learning that extends from peer review and implementation is a more important tool of change than threats of blacklisting or financial punishment. Thus, FATF has been most effective at extending the AML regime when members have used it in line with the principles of experimentalist governance. States and professions subject to FATF’s work have pushed back the most when material power became a primary tool of change. This interpretation challenges the existing common understanding of the importance of blacklisting within the regime and suggests a very different set of reforms that FATF members should consider going forward. Put most simply, bolstering enforcement within FATF is likely to be counter-productive, while reinforcing social learning and peer review are more likely to generate greater returns.

Question 2: Is FATF a financial or security network? To what effect?

Especially as FATF expanded into counter-terrorism financing in 2001, it created an important and as-yet unresolved tension. Is anti-money laundering and the work of FATF aimed at shoring up the financial system and protecting those invested in the system from abuse? Or has FATF become fundamentally a tool of security actors, aimed more at national security and, to a lesser degree, criminality? Two authors here provide two different interpretations, but both emphasize that balancing the two sides has been a challenge.

Anthony Amicelle argues that the AML must be understood as a “configuration,” or a social space characterized by a “tension-balance” between interdependent actors. As a result of AML, banking and law enforcement officials regularly must work together, but they bring with them different frames of reference. Security actors tend to see their jobs as ensuring national security and defending against societal risks over any other end, while financial actors see themselves as ensuring financial integrity and defending against institutional risks. Despite that, the interactions generate a “productive misunderstanding” that allows them to cooperate as if they agreed. Ultimately, however, this productive misunderstanding is embodied in the person of the compliance officer, and those officers work for the financial side, not the security side. So while security and financial officials in the UK and Canada, Amicelle’s two cases, cooperate in both formal and informal ways “to an extent inconceivable ten years ago,” the balance tips in favor of the financial actors. FATF and AML have led to the securitization of the financial sector, but the greater change, argues Amicelle, has been the financialization of security.

Anja Jakobi continues her work in comparing the governance of different transnational crimes. In this special issue she merges theoretical concepts from criminology—which often focuses on the domestic, policing side of crime—with insights from

International Relations—which focuses more on the interaction of actors at or above the level of the nation-state. From this she builds an analytical framework that highlights five dimensions of security governance: a comprehensive security concept, multi-purpose rationalization, public-private cooperation, multi-nodal governance, and transnational security spaces. Using this framework, she points out that FATF members were successful in advancing the AML agenda in all of these aspects of security governance. This explains why the AML regime moved forward more than many observers initially expected. At the same time, it also explains variation within FATF: why some initiatives moved forward more than others. Those initiatives with a tie to security developed more than those that focused only on financial integrity. So while analysts often present FATF as a financial regulatory body, in fact FATF is better considered an instrument of security governance. AML, she writes, “is still a weak governance instrument for regulating financial crimes such as tax evasion or corruption, but it’s a strong one for security-related crimes.” This conceptualization provides other norm or organizational entrepreneurs with a roadmap toward greater prominence within the regime.

Question 3: What role does, and should, the private sector play?

Scholars have not researched the role of the private sector in FATF and the AML regime as thoroughly as one might expect, although there are important exceptions. This is perhaps because of the prominence of state-based explanations cited above, but those only raise more compelling questions. If state interests drive FATF and the AML regime, how have the interests of private financial sector played into those state preferences? Drezner [20] argues that financial instability in the 1990s left wealthy U.S. and European investors eager to re-regulate finance in exchange for financial stability. That may have bolstered the regime’s growth, but it ignores the fact that the regime got its start (in 1989) before the financial crises of the 1990s could shape investor preferences. Sharman’s work suggests that state preferences break along the lines of the emphasis of the domestic financial sector; states with financial sectors built around stability preferred stronger AML rules, while those built around secrecy preferred less scrutiny. Little work, however, has systematically traced the empirical footprints of those arguments to connect them to outcomes. The scholarship of some of the authors in this special issue provides a corrective to this long-standing gap.

Eleni Tsingou’s article here highlights the evolution of the compliance industry, in particular. She writes that compliance professionals not only are the “foot soldiers in the fight against money laundering,” but have evolved from being rule takers to rule makers. While previous work has looked at national cases of the compliance industry [31–34], Tsingou draws on interviews and participant observation in making the global compliance industry her unit of analysis. Its professionalization, she writes here, “has led to an extension of governance functions, from implementation, to active interpretation of rules, to shaping the content of governance through regulatory creep.” This transformation, and empowerment, of the compliance profession has happened at the highest levels because of the revolving door between regulators and banks. It has happened in the small numbers of firms that provide IT and other technical capacity to financial institutions. It has even filtered down to the junior- and mid-level officer level, where the development of internationally recognized qualifications, an international

conference and workshop conference, and north-to-south capacity building efforts drive convergence. The result is a deeply transformed aspect of the AML regime, which feeds into FATF and the standard-setting process. An important implication of her argument is that we will not be able to understand FATF and the AML regime going forward without giving the compliance industry in particular primacy of place in our models.

Karin Svedberg Helgesson and Ulrike Mörth have worked to understand the role of “frontline” private sector actors outside the compliance industry. In their contribution to this volume, they draw on interviews with lawyers in Sweden to understand how FATF’s rules addressing the legal profession trickle down to the day-to-day practice of law and how lawyers respond. The legal profession has been skeptical of AML from the beginning. Lawyers fear that AML regulations impinge on attorney-client privilege and inhibit their ability to provide their clients with the best possible defense.⁹ AML experts, however, fear that attorney-client privilege allows lawyers to help their clients launder money and hide behind privilege. Helgesson and Mörth emphasize that the new risk-based approach entails important assumptions about the nature of AML and the role these actors can and will play. It places increased responsibility on private actors, assumes that the risks of AML are knowable to those actors, and implies that those actors can and will act in line with the intentions of the standard-setter. In the Swedish case, law firms have developed “practices of separation” that allow them to navigate the shoals of FATF standards, on one side, and professional and business obligations and goals on the other. The result is a business-oriented pragmatism on the part of the legal profession, rather than a more productive engagement as we see even in some banking sectors. The authors argue that FATF members have not contextualized standards sufficiently to generate rules that appropriately distinguish between the banking and non-banking sectors, an important question for practitioners going forward.

The contribution by Peter Romaniuk and Tom Keatinge reveals a different path for private-sector involvement, but generates another call for sector-based contextualization. They provide a fascinating look at how the non-profit sector ended up involved in AML. Following the 2001 terrorist attacks in New York City, some FATF members, led by the United States, pushed hard to include a special emphasis on counter-terrorism financing. In service of that goal, members added eight so-called “Special Recommendations” (SR) in October 2001, before adding a ninth in 2004. It was arguably at this point in history that FATF and its newly named “40 + 9 Recommendations” became best known. SR8 addressed concerns that charities were serving as laundering agents for terrorist groups. With time, however, it became clear that states’ efforts to comply with SR8 were threatening the viability of the “third sector,” which was so vital to development and human security around the world. Romaniuk and Keatinge document how a “transnational advocacy network” [35] formed and worked successfully to re-frame the issue in terms of rights and proportionality. FATF members revised and re-issued SR8 in 2016. They also created a consultative forum for NPOs like that created

⁹ At the time of writing, for example, journalists reported that Joaquín “El Chapo” Guzmán was struggling to hire a defense attorney, in part because lawyers fear that they could be found guilty of money laundering (i.e., knowingly receiving profits from illicit activity) should El Chapo be found guilty. <https://www.wsj.com/articles/latest-legal-woes-for-el-chapo-paying-for-a-lawyer-1499079600>. Accessed July 6, 2017.

for the private sector some years earlier. The outcomes and the path to success, they argue, provides a playbook for other sectors affected by FATF's expanding activity. The case also holds an important lesson for FATF about the need for consultation and contextualization before issuing potentially harmful recommendations.

Question 4: How responsive is FATF and the AML regime?

Most of the articles cited thus far stress how FATF has changed over time. But how responsive is FATF to the changing world around it? It is a pressing question. The 2008 crisis confirmed that financial innovation can outpace our understanding of the implications of those innovations [36]. This is particularly true in the adaptive environment of illicit markets. As with the other themes, many of the papers address this question indirectly or briefly. Two papers take on the question more squarely.

One way to think about responsiveness is the ability of FATF recommendations to apply and be effective in different contexts. I argue that the experimentalism of FATF should make it more adaptable and flexible, but William Vlcek in this volume suggests it may not go far enough. AML stretched more deeply into informal economies, he argues, because of displacement; AML drove money laundering out of formal economies, which made informal economies more attractive. But FATF's reliance on typologies, or the development of AML guidance in response to specific patterns of money laundering, renders the system less adaptive and more rules-based than some analyses suggest. De-risking only exacerbates the problem, as it forces still more economic activity into the informal, less observable realm of the market. As an operable piece of advice, he writes that calls for formalizing informal economic actors are often "beyond the means and ability of the state in question." There may be technological fixes that minimize reliance on human resource, but he also reminds would-be enforcers that those fixes "require resources and institutional capacity to maintain." Capacity-building assistance—beyond sharing ideas and stretching into funding—might be an area that FATF members should give greater priority.

A second vector of adaptability addresses FATF's capacity to respond to new means of money laundering. Malcolm Campbell-Verduyn considers whether FATF and the AML regime have responded appropriately to "crypto-coins," such as Bitcoin. Many major financial institutions remain leery of them as standard currencies. For money laundering and illicit economies, however, crypto-currencies remain an important new frontier. "Altcoins" are "verified through decentralized peer-to-peer networks and then broadcast on public ledger that encode the transaction histories of each individual crypto-coin." As such, they effectively by-pass most AML actors. They are quasi-anonymous, which frustrates the Know-Your-Customer principles at the heart of the AML regime. Monitoring their use is also difficult, which makes it difficult for investors and regulators to identify normal versus abnormal patterns. If FATF's sole goal with crypto-currencies is to prevent money laundering, he argues that FATF's guidance on the question falls short. It relies too heavily on private industry to regulate itself, promotes a technological arms race around anonymity between regulators and users, and emphasizes high-risk exchanges while overlooking the "middlemen" down the chain that have major financial incentives to verify suspicious transactions. That said, these governance gaps may not be fatal, because quasi-anonymity is only one of two blockchain pillars. The other is that every transaction with a "coin" is visible.

Quasi-anonymity might prove a loss, but the development of currencies that carry their own logbook of transactions might prove a gain. There is a widening field of companies competing to provide crypto-currency forensics to police. “Permissioned blockchains” actually build in user identification, making them especially good for meeting Know-Your-Customer standards, while saving customers and financial institutions resources. The Isle of Man appears to be developing a comparative advantage in hosting AML-compliant, more reputable crypto-currency companies. Especially in relation to better established, “lower-tech” forms of money laundering, argues Campbell-Verduyn, the blockchain technologies of crypto-currencies likely provide a greater advantage to AML in the long-run. An important question moving forward is whether FATF and the AML regime can adapt to take advantage of this technology.

Question 5: Is FATF effective? How can we know?

Finally, the most important question that the articles here raise is the question of effectiveness. Every article in this special issue has something important to say about the question. It is also the question that FATF members have wrestled with the most in the past five years and, hopefully, the one they will be wrestling with in the years to come.

Readers of this journal are aware that the question of effectiveness is always difficult in social science research. Part of this has to do with the complexity of social phenomena and the slippery nature of causality in such settings. In *International Relations*, a debate relevant to this special issue focused on the impact of international institutions and why states tend to comply with their international obligations [37]. For some, compliance was an indicator that international institutions (understood in the field to include most any agreement among states) mattered [38–40]. International institutions and the process of building them were capable of shaping participants’ identity in ways that brought their preferences in line with the goals of the institution. Institutions could facilitate persuasion and socialization amongst their members [41]. Critics argued that compliance stemmed from the fact that most international institutions were merely codifications of pre-aligned preferences. Institutions did not cause convergence, they only reflected it [42]. These “enforcement school” scholars argued that any agreement requiring states to veer very far from their top preferences also would require strong enforcement by leading states. Do institutions “cause” preferences to align, or do aligned preferences “cause” institutions? Counterfactual reasoning is also important: would the problem have been worse without the institution and how do we know?

The questions map well onto FATF. They may even be more difficult. If the fundamental problem of causality is complex in all social science inquiry, the challenge becomes greater still in studying illicit activity. Numbers are notoriously unreliable. The collection of papers in Andreas and Greenhill [43]’s *Sex, Drugs, and Body Counts* vividly illustrate the problem.

A second problem is that scholars often use the word “effectiveness” to signify different concepts. Here the important divide is between what I will describe as endogenous or exogenous conceptualizations. Endogenous understandings define effectiveness according to the more immediate goals of the institution. Exogenous understandings focus instead on the impact an institution has on larger problem members understand the institution as addressing.

In the case of FATF, an endogenous approach might measure the diffusion of AML rules or the prioritization of AML. Are states getting the correct laws on the books? Are they implementing those laws? The exogenous conceptualization, in theory, is more straightforward: Is the AML regime slowing the amount of money being laundered?

Until the most recent round of mutual evaluations, FATF members used an endogenous definition. This approach is easy to critique. FATF might be perfectly effective at diffusing perfectly ineffective rules. Consider, however, the counterfactual: if FATF had the perfect rules for a perfect AML system but was unable to diffuse those rules, the AML regime would still be ineffective. Diffusing standards is a necessary, although insufficient, condition for an effective AML regime. Most of the themes above can be thought of as endogenous indicators of effectiveness. I briefly highlight three especially prevalent ones, re-treading some ground covered above to place the questions in the context of effectiveness.

The first is participation. Who should participate in FATF decision-making and what role should they play? Romaniuk and Keatinge show the dangers of simply imposing rules without consultation, but Tsingou's work suggests that the AML regime may be susceptible to regulatory capture by the compliance industry. Nonetheless, many of the authors also make it clear that the private sector, both for-profit and non-profit, has a role to play. One measure of FATF's effectiveness, therefore, would be to gauge that role. Does FATF consult them without bending to them? Does the private sector generally accept the outcomes of the governance process, even when the rules promulgated cut against their preferences? Are only service providers included, or are consumer advocates at the table, too? What about private sector representatives from all levels of markets, from developing to developed? What role is there for private sector security actors?

The second important theme regarding endogenous effectiveness sits somewhat in tension with the first, namely the ability to adapt to new challenges. With its focus on financial integrity, how effective is FATF at identifying and responding to new forms of money laundering?¹⁰ The tension with a participatory understanding of effectiveness lies in the numbers. On one hand, increased participation brings greater experience, wisdom, and insight from the "front line" that would help identify and respond to challenges. At the same time, too many voices create a din from which it is hard to create order. The balance that FATF members must strike is between front-line experience and an efficient, independent decision-making process.

A third aspect of effectiveness is FATF's adaptability to different contexts, which nearly every article addresses in some way. If one goal of FATF is to promote financial integrity while still encouraging financial innovation and growth, that no doubt calls for ensuring that jurisdictions adapt FATF's 40 Recommendations to their local context. The risk-based approach (RBA) to AML in theory helps insulate the regime against one-size-fits-all approaches, but the RBA is far from settled practice in FATF. Members therefore could incorporate the implementation of a risk-based approach to AML as a partial

¹⁰ Identifying new challenges and responding to them are not the same and probably deserve their own lines of analyses. For the sake of space, I refrain from that here except to note that the field needs more research on the ability of FATF and similar institutions to identify new challenges, not only on how they respond to problems. In FATF, the typologies exercises are important loci for this kind of creativity. Cross-institutional comparisons would be a good place to start for such investigations. For an example of both, see Sharman [44] on the replication of error through diffusion.

marker of broader adaptability. Highlighting the interconnectivity among these angles of effectiveness, one way to promote adaptability of FATF's standards is to ensure that participants in all FATF fora represent a broad array of development levels. In this regard the inclusion of the FATF-style Regional Bodies as associate members is a step in the right direction. Ultimately, it may do more to highlight their second-class status than to ensure that they are able to contribute to a more adaptable, more effective FATF. As the network grows, however, there is a danger that the Recommendations become top-down regulations. That cuts directly against the idea of contextualized adaptation.

While the exogenous definition of effectiveness is conceptually more straightforward—whether or not money laundering is less common—there are several serious obstacles to measuring that variable. The best example is a metric used by FATF itself: the number of money laundering convictions in a jurisdiction. FATF is critical of jurisdictions that do not show an increasing number of convictions. The problem with that measure is that a jurisdiction with the perfect AML system and a jurisdiction with no AML system would yield the same number of convictions: zero. In more nuanced terms, a strong AML system should generate a decreasing number of convictions as deterrence takes effect, but so would a weakening AML system, as fewer launderers are prosecuted. In reality, the number of convictions matters only relative to the number of times someone tries to launder money, but we do not have that baseline measurement. If we do not know the starting line, it is difficult to know how far we have come.

That said, reliable data is a problem in most any field, especially in the early phases of inquiry. The key is to begin gathering better data. That seems especially true in a field like international finance, which in so many ways is about the creative construction, production, and utilization of data. What the field needs—both the academic field and the field of practice—is a more concerted effort to solve the data problem. There are good examples of partial measures. Robert Kudrle [45], for example, has examined whether blacklisting leads to any demonstrable financial impact. He finds it has not. Importantly, that does not mean that FATF is in effective overall, but that blacklisting may not be a primary mechanism of effectiveness. Jason Sharman [23] conducts a bold experiment to see how easily he can open anonymous shell companies, in direct contradiction of FATF standards. He finds that it is disturbingly easy. These two works are excellent examples of the kind of research and oversight that the AML regime needs if we are interested in an exogenous understanding of effectiveness. In this same vein, the best measure is probably to track the price of money laundering. What premium do institutions charge for breaking AML regulations? Research and analysis that focuses on direct measures, however, remains the exception to the rule.

It is on this point that Michael Levi, Peter Reuter, and Terence Halliday take FATF to task in the final article of this special issue. They provide one of the first assessments of FATF's efforts to measure its own impact on money laundering. They begin with the 3rd round of mutual evaluations, which included a provisional attempt to prompt thinking on AML effectiveness. The reports, they write, are inconsistent and incomparable. In reporting on the efficacy of Suspicious Activity Reports (SARs) systems, for example, Levi, et al., note that the evaluations ignore that some states have a threshold-based automatic reporting system, while others rely on human analysis to identify odd-seeming transactions. The result is that analysts can do little with the data on the numbers of SARs. Nor do the reports provide any qualitative assessment of the legal follow-ups to the SARs, which the authors note is probably more important than

the numbers of reports generated. A lack of comparable data on outcomes makes learning even more difficult.

The 4th round evaluations, which have just started, do not promise to be much better. Levi et al., consider the National Risk Assessments, which are to establish the kinds of money laundering that are most likely in a state and serve as a guide in future evaluations. The reports require substantial cross-sectoral collaboration within a country, which is positive, but the content of the reports to date is not promising. The reports vary in quality and format. Most seemed to be simple aggregations of widely available data in acritical and irregular forms. As Levi et al., write: “The NRA, admittedly in its initial implementation, suggests how weakly FATF has articulated the role of data and data analysis in the assessment process and/or how modest have been the attempts to implement that requirement.” The NRAs to date seem to be a shaky foundation upon which to build an effort to judge FATF’s effectiveness going forward.

FATF leadership has been frank about the fact that measuring effectiveness will be difficult. No one disagrees with the point, but it verges on becoming a “common sense” truth that escapes scrutiny. The difficulty of gathering data on illicit finance should not stand as an excuse to stop trying. Like weather forecasting, we can only begin to identify meaningful patterns within the data after we have enough data points to consider.¹¹ Recall the problem with using the number of money laundering convictions as a marker of effectiveness. If we begin gathering data on that question (including historical data), we can begin to establish common patterns. Do they go steadily up as AML implementation advances? Is it an arch that sees numbers go up, then down? Is it a concave, but upward sloping curve, that sees an overall increase, but with a declining rate of increase after a certain point? Or is there no change? Comparisons with other crime rate analysis also would seem to be a productive project. Building the database that is required to better measure the effectiveness of FATF and the AML regime is no doubt a massive, multifaceted undertaking. It requires theorization about the variables that are most likely to matter and actually gathering the data. It is bound to be an inefficient, pragmatic process. It is also where the private sector might be compelled to participate more directly. Acknowledging the challenges of trade secrecy and client privacy, relevant financial and non-financial institutions should be sharing data, as should software companies that develop tools for AML compliance (and which therefore have data about patterns of financial flows). It also is a question that should see much greater engagement between academic analysts and practitioners.

Ultimately, the best measure of effectiveness is one that includes both endogenous and exogenous measures. The importance of legitimacy in promoting compliance is perhaps the best example that the two conceptualizations are different sides of the same coin [21]. Just as neither GDP growth nor unemployment reflect the health of the economy, no single metric will fully measure the relative efficacy of FATF and the AML regime. Nearly three decades into FATF’s life, however, we are long overdue for a sustained dialogue on developing meaningful, multifaceted measures of effectiveness.

¹¹ The history of weather forecasting is a useful history in this regard. See, for example, Harper [46]. For a much shorter history, see: <https://earthobservatory.nasa.gov/Features/WxForecasting/wx.php>.

Conclusion

As is true of the broader project, this introduction does not claim to fully reflect every question related to FATF and the AML that scholars have delved into since FATF's founding. Its aims are more forward-looking. One aim is to give a wider community of scholars a quick primer on an important and understudied institution, the Financial Action Task Force, and the AML regime it has built. The second is to encourage that audience to dive into and digest the scholarship in the pages to follow. As I argue in my article to follow, FATF once seemed like an outlier in the system, worthy of study because it was unusual. Increasingly, however, the governance of transnational problems is transforming to look more like the multi-level, public-private, issue-focused regime that FATF has built. In that regard, it contains the potential to shed light on questions relevant to any number of fields.

At the same time, FATF members themselves seem aware of being at a crossroads, having seen the regime mature from a temporary, ill-defined task force into a major international governance institution. It is more important than ever that academics contribute their insights to the regime in order to make it a more equitable, more legitimate, and more effective governance system. The articles included in this special issue, both individually and as a whole, have the potential to do that. The scholars whose work comprise this special issue may not agree on a reform agenda for FATF, but all believe that FATF is a significant body in transnational politics. It matters on macro-scale, where questions of international cooperation and system integrity and stability are in play. It matters on a micro-scale, where financial regulation affects access to credit and the functioning of financial markets that have such a substantial, and varying, impact on economic development. In that vein, and as a final aim, I hope the articles to follow will shape the research agenda on FATF and the AML regime in the years to come. I also hope that people working in AML will eventually take in the collective insight offered here to shape the AML agenda going forward. FATF's reach is too far and its topic too important to keep it isolated from outside critique.

As a final word, this special issue has been in progress since 2014, when Anja Jakobi, Eleni Tsingou, and I first began discussing it. Jakobi and Tsingou received a workshop grant in 2015 from the International Studies Association conference where some of the authors presented their work. Peter Andreas, Patrick Cottrell, and Chip Poncy presented valuable feedback at that workshop. One year later, all of the authors presented papers at a 2-day workshop graciously hosted by the Americas Center at the Federal Reserve Bank of Atlanta and partially underwritten by North Carolina State University's School of Public and International Affairs. This project likely would not have come to fruition were it not for that support, and so on behalf of the authors I thank both of those institutions. Thomas Biersteker, Lori Crasnic, Sue Eckert, Jessica Morse, Abe Newman, and Jason Sharman participated in that workshop and helped all the authors here sharpen their arguments. Steven Kay at the Federal Reserve of Atlanta strongly supported this project, simply because he felt the topic deserved greater attention. He and his team, including Vanessa Jordan and Tamara McLaurin, deserve a special word of thanks. I hope it proves to have been worth the effort. Thanks also are due to Nikos Passas, the editor of *Crime, Law, and Social Change*, for his enthusiasm, and to Kathleen Krzyzanowski for her editorial assistance. The contributing authors, of course, deserve the greatest thanks for their contributions.

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