

Examinations of Allegation on Non-Compliance with AML/CFT Laws to Islamic Banking

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Abstract. *The dangerous dimension which the terrorism financing incursion introduced to peace and harmonious life globally, makes the issue of money laundering and combatting financing terrorism (AML/CFT) a serious phenomenon. The compliance with the AML/CFT laws now generates global interest. Assessment of whether Islamic banks are complying with AML/CFT compliance measures becomes a grave issue that require attention particularly against the background of allegation by Western countries of lax control and supervision. This is probably because of the havoc that the world has continuously experiencing as a result of these menace. The issue has continued to come in different dimensions and like a Siamese twin, the banks have become the focal point and inseparable in the issue of how to combat this menace. Incidentally, the increase in the growth and development of Islamic banks across the globe has dragged it to the centre of discussion. Thus, there have being a recurring issue on Islamic financial institutions regarding its compliance with Anti-money laundering laws and Combating Financing Terrorism (AML/CFT) measures. There were allegations of non-compliance with AMLCFT laws by Islamic banks, particularly by some Western countries led by the United States of America. Consequently, the issue of combatting money laundering and terrorism has become a major issue in the global domain. This paper has extensively examined the allegation of non-compliance of Islamic banks with AML/ CFT laws. This is done by beaming searching light on the growing perception of lax in the control, monitoring, weak supervision, and non-compliance of Islamic banks with AML/CFT measures that is been spearheaded by some western countries, led by the US. Thus, by using the doctrinal research methodology, the paper sought to determine the veracity of the allegation and incidentally found that the allegation is not only baseless but lacks empirical evidence.*

Keywords: Islamic Banking; Non-compliance; Money Laundering and Terrorism Financing.

1. INTRODUCTION

Banks generally are not immune to the ever-growing money laundering and financing terrorism risk. Islamic banks are however tagged by some western countries to be more vulnerable to launderers without any empirical findings to suggest that Islamic banking, compared to conventional banking posed more money laundering and terrorism financing risks. Consequently, the need to examine the veracity of Islamic banks adherence to Anti-Money Laundering and Combating Terrorism Financing (AML/CFT) laws becomes necessary and desirable. This is because, issue of banks' compliance with money laundering and counter financing terrorism laws (AML/CFT)

have become critical and focal point whenever there is discussion on how to combat the menace. Moreover, this has become a recurring scenario and such stands are likely to be justified if the sensitive position occupied by banking sector is considered. The functionality of the banking sector (is firmly belief to) have direct link with the economy growth and development of any nation and compliance with AML/CFT by banks therefore becomes a major area that must be addressed. This is because the consequential effect of AML/CFT has a wider implication on the economy, survival, security, and the sustain-ace of every nation. Particularly, when it has been proven severally that banking sectors are not immune from being used as conduit.

It is a common view that ensuring compliance with AML/CFT laws (without any doubt) attracts huge resources. However, despite the huge investment in this regard (in many countries), there are still elements of compromises, market manipulation and rigging standards all over on the part of banks. Consequently, ensuring an effective and efficient supervision of financial institutions and orderly conduct of financial system become vital. This is probably because achieving meaningful growth and developments appears to have correlative relationship with ability to prevent leakages, level of corrupt practices and many other money laundering predicate offences. Therefore, the thought of combating AML/CFT in most cases are backed up with effective plans to prevent the use of financial institutions facilities for the purpose of committing crimes. Thus, combating AML/CFT through compliance with the internationally acceptable measures and enforcement of the required AML/CFT legislations and regulation are key for the overall development of every nation's economy and safeguarding the financial integrity.

Incidentally, the world has begun to witness significant contributions of Islamic finance to the global financial system. Moreover, the increase in the growth and development of Islamic finances across the globe is probably making focus on Islamic banking to be on the increase and its compliance with AML/CFT is therefore raising lot of concern.

2. RESEARCH METHODS

The approach method used is literature research which Weiss on his part in 2005 found that terrorists seek increasingly more informal methods of earning and moving money. He concluded by opined that the financial support and earning funds of terrorist groups are a combination of fund generated through both legal and illegal means and serious engagement in illicit movement of money for terrorism financing through jurisdictions with a weak AML/CFT legal regime.¹

3. RESULTS AND DISCUSSION

3.1. Islamic Banking

Islamic banking is a banking system that complies with the Sharia dictum. It is one of the main products of Islamic finance and its non-interest system distinguished it from

¹ James B Bexley, Balasundram Maniam, and Joe F James, "Perception of Islamic Financial System: Its Obstacles in Application, and Its Market," in *Allied Academies International Conference. Academy of Accounting and Financial Studies. Proceedings*, vol. 5 (Jordan Whitney Enterprises, Inc, 2000), 1. See also Kostas Drakos and Andreas Gofas, "The Determinants of Terrorist Activity: A Simple Model for Attack Occurrence across Space and Time," in *Conference on the Political Economy of Terrorism, University of Southern California*, 2004.

all other form of banking operations. This implies that it is a practical demonstration of Sharia. It therefore constitutes a new phenomenon in banking sector that takes the whole world in surprise.² Despite its relatively new age compared to the conventional banking, the Islamic banking sector has spread like wildfire to almost all the continents of the world. Its fast growth globally might probably constitute one of the factors that is creating a sort of suspicious feelings and negative perception about Islamic banks. This negative perception is unfortunately gaining more ground.

Currently, there is a USA Governmental agency led allegation that Islamic banks are more vulnerable to money laundering and terrorism financing, because of its perceived lax control and supervision (of AML/CFT) in Islamic banks. This inference could be drawn, because Islamic banking sector presently constitutes about 80% of the entire Islamic financial industry with estimated assets of more than US\$1.4 trillion³ globally and the number of Islamic Banking institutions is presently over 400⁴.

3.2. Perceptual Issue

There are two major areas which has attracted (mostly negative) comments, reactions, and criticism internationally. These areas are money laundering and terrorism financing. There have being a recurring issue on Islamic financial institutions, particularly the banking sector, regarding its compliance with Anti-money laundering laws and Combating Financing Terrorism (AML/CFT) measures. The operation of Islamic banks is considered by some countries particularly the United States of America (USA) to be prone to non-compliance with AML/CFT measures. The stand of the USA and its allied has always been that there is laxity in the supervision of money laundering legislations and regulations particularly with Islamic banks. The issue of terrorism financing also becomes more pronounced after September 11 terror attack on the USA.

What led to this perception is difficult to understand. Although, different opinions and suggestions have been offered. While most scholars such as Norman⁵, Norhashimah,⁶ Scneider, Yazid⁷ and Nasir⁸ are unanimous in relating terror attacks believed to have been orchestrated by some radical Muslims as the root cause of the negative perception. There are yet some other view canvassed by other scholars. For instance, Yazid Zul Kepli suggested that the negative perception is a product of Islamophobia by the western countries,⁹ while Nasir concluded that the inability of the international regulatory agencies such as FATF, WOLFSBERG and others to facilitate reasonable research paper and study on Islamic finance products precluded many from

² Mohamed Ariff, *Islamic Banking*, 1988. Ariff, Mohamed. "Islamic Banking." *Asian-Pacific Economic Literature* 2, no. 2 (1988): 48-64.

³Ibid

⁴ Islamic Finance Services Board Stability Report cited in IMF Working Paper WP/15/XX

⁵ Normah Omar, "Terrorist Financing and Perceptions on Islamic Financial Institutions," 2010.

⁶ Norhashimah Mohd Yasin, "Regulation of Islamic Banks and Allegations of Lax Control of Money-Laundering," *Journal of Islamic Law Review* 4 (2008).

⁷ Yazid Mohd Bin Kepli, "The Common Mistakes in Combating Terrorism Financing," *International Journal of Business, Economic and Law* 10, no. 2 (2016).

⁸ Maruf Adeniyi Nasir, "Anti-Money Laundering Laws: The Sharia Perspectives," in *International Seminar on Islamic Jurisprudence in Contemporary Society* (Kuala Terengganu, Malaysia: Universiti Sultan Zainal Abidin, 2017).

⁹ Yazid Mohd Bin Kepli, "The Common Mistakes in Combating Terrorism Financing."

understand the positive sides and benefit of Islamic finance products.¹⁰ Invariably, lack of adequate knowledge about Islam and Islamic financial system is a major challenge.

Although, the act of terror is not limited to a religion or group, but it appears that the event of terror attacks appeared to have had overriding influence on the psyche of many. It has also created some ill feelings and negative impression more about Islam and most importantly the Islamic banks and other financial institutions. Some of these happenings include the "terrorist attacks of the United States (US) World Trade Centre on September 11, 2001; Bali bombings in 2002 and 2005; London Bombing in 2005; and the Mumbai bombing in 2008."¹¹

All these had left some negative impression and a very detrimental global perception impacts on the Muslims and Islamic financial institutions globally. This is because, most of these attacks were believed to have been carried out by some militant Islamicists. A lot of public scepticism were therefore, understandably, against the Muslims and the religion of Islam' Invariably, there are now increase feelings that have culminated into allegations among the western countries that Islamic banking institutions (IBI) are not only vulnerable but are serving as conduit or linked in one way or the other to money laundering and terrorism financing.¹²

Consequently, the spotlight has been consistent in its focus on Islamic banking institutions (IBI) role in money laundering and terrorism financing¹³. The regulatory and supervisory regime were alleged to be weak when compared to conventional banking and already compromised given room for its manipulation by the ever-sophisticated launderers.¹⁴ A noticeable issue that make support for an empirical study a desirable one is that this assumption appears to have been generalised. A sort of blanket allegation is now spreading against Islamic banks and Muslim country without any exception.¹⁵

A classic example of such negative perception is a statement that emanated from a United States of America's Governmental Agency. The US law enforcement agency probably because of the attack on the 11th of September 2001 made some conclusive statements that are pointing to the fact that regulations of Islamic banks is lax, and exception is not given to any Muslim countries where Islamic banks are operational, rather it was an allegation that was generalised.¹⁶ In a report released by the US state Department, the following statements were made:

¹⁰ Maruf Adeniyi Nasir, "Global Perspectives on AML/CFT Risks in Islamic Banking Institutions: Facts or Fallacy?," in *6th International Conference on Islamic Jurisprudence in the 21st Century* (Kuala Lumpur, Malaysia., 2017), 544–58.

¹¹ Omar, "Terrorist Financing and Perceptions on Islamic Financial Institutions."

¹² Maruf Adeniyi Nasir, "Islamic Finance and Anti-Money Laundering: A Myth or Reality?," in *5TH ASEAN University International Conference on Islamic Finance* (Jerudong, Brunei Darussalam, 2017), 61–73.

¹³ Norhashimah Mohd Yasin, Regulation of Islamic Banks and Allegations of Lax Control of Money La.undering, *Journal of Islamic Law Review vol 4 (2008)*, pp107-119.

¹⁴ Norhashima Mohd Yasin and Yazid Mohd bin Kepli Maruf Adeniyi Nasir, "Anti-Money Laundering (AML) Legal Framework: The Shari'ah Perspective," *Journal of Islamic Law Review* 13, no. No. 2 (2017): 211–32.

¹⁵Ibid

¹⁶ Norhashimah Mohd Yasin, Malaysian Islamic Banking Regulation in Relation to Anti-Money Laundering and Counter Financing of Terrorism (AML/CFT): the Aftermath of Islamic Financial

Some terrorist groups may also use Islamic Banks to move funds. Islamic banks operate within Islamic Law, which prohibit the payment of interest and certain other activities. They are proliferated throughout Africa, Asia and the Middle East since the mid-1970s. Some of the largest Islamic financial institutions now operate investment houses in Europe and elsewhere. Many of these banks are not subject to a wide range of anti-money laundering regulations and controls normally imposed on secular commercial banks nor do they undergo the regulatory or supervisory scrutiny by bank regulators via periodic bank examinations or inspections. While these banks may voluntarily comply with banking regulations, and in particular, anti-money laundering guidelines, there is often no control mechanism to assure such compliance or the implementation of updated anti-money laundering policies.¹⁷

This gives impression that the Islamic banking institutions are not been properly supervised like its conventional counterpart. The perception was promoted and spread by some western countries. It became more pronounced as result of peak interest of post America September 11th, 2001, experience and ever since then the study of money laundering and terrorist financing risk in Islamic finance has attracted relatively little attention.¹⁸

Strengthening the fact that the 'public negative perceptions towards the religion of Islam and Muslims are not a myth.' Normah confirmed that:

In fact, a 2006's post 9/11 poll conducted by the ABC News and the Washington Post presents clear documentary evidence which revealed that 46% of Americans expressed an unfavourable opinion of Islam. Describing the same survey, Ali, S. N & Syed A.R (2010) further noted the findings of the poll stated that six out of ten Americans believed that Islam was "prone to violent extremism"; and another 25% of those surveyed also admitted to "prejudicial feelings" against Muslims and Arabs. The negative perceptions had indeed double that of a similar survey conducted in 2002.¹⁹

This perception of lax and non-compliance is still significantly based on assumptions that have not been empirically proved²⁰. Consequently, determining the veracity of such opinion and feelings becomes necessary to put the issue in the right perspective. Meanwhile, because of this kind of thought and reasonings, Islamic charity accounts in many Muslim countries (and even other countries with very few Muslims population)

Services Act 2013 (IFSA). A Chapter in edited work of, Adnan Trakic and Hanifah Haydar Ali Tajuddin, *Islamic Banking & Finance: Principles, Instruments & Operations* (Second Edition, CLJ Publication, p. 455-476.).

¹⁷International Narcotics Control Strategy Report, Bureau for International Narcotics and Law Enforcement Affairs, State.

¹⁸ Nadim Kyriakos-Saad et al., "Islamic Finance and Anti-Money Laundering and Combating the Financing of Terrorism (AML/CFT)," 2016.

¹⁹ Omar, "Terrorist Financing and Perceptions on Islamic Financial Institutions." See also Jamaliah Said et al., "Money Laundering Prevention Measures among Commercial Banks in Malaysia," *International Journal of Business and Social Science* 4, no. 5 (2013).

²⁰ Nasir, "Global Perspectives on AML/CFT Risks in Islamic Banking Institutions: Facts or Fallacy?"

have been experiencing sharp discrimination.²¹In many countries of the world such as United Kingdom and United States of America, many Muslim groups account have been closed and banks are withdrawing services to many others.²²

The growth of Islamic finances in the recent past makes the compliance of Islamic banks with AML/CFT to be of immense importance in line with the global trend on AML/CFT.²³ The subsequent segment therefore focusses on the literature review of various scholarly views, comments and opinions on the level of Islamic banks compliance with AML/CFT to bring out the current thought and perspectives on Islamic banks and particularly in Islamic countries. Views on the alleged non-compliance of Islamic banks with AML/CFT measures will therefore be examined.

It is worthy of note that the phenomenon of money laundering and combating the financing terrorism (AML/CFT) has attracted several scholarly contributions most especially on the risks that are associated with conventional banking or finance.²⁴ However, the potential money laundering and financing terrorism (ML/TF) risks in term of its applicability and compliance with international standard have attracted few literatures.²⁵While the conceptual analysis of money laundering and its effects as well as that of Islamic banks have been fully discussed in various perspectives the issues of Islamic banks compliance with anti-money laundering/combating financing terrorism (AML/CFT) laws and regulations attracted least contributions.²⁶

Perceptual assessment regarding Islamic banks would, therefore, necessarily require a careful analysis of earlier studies and scholarly works on Islamic banks. Particularly as it relates to compliance with money laundering and terrorism financing laws. The basis for negative views on Islamic finance and particularly the Islamic banks which includes allegation of lax control and non-compliance with money laundering 'laws and regulations' must therefore be subjected to scrutiny and the basis or justification (if any) for perceptual consideration, or such opinion must be established.

To some scholars, such views are product of enviable records of positive development and growth that are being recorded globally by the Islamic financial products. While sukuk has gradually becomes a potent financial instrument that has been embraced in many countries of the world, Islamic financial institutions particularly the Islamic banks is also fast becoming a major stakeholder in the global financial system. This is evident in the rate of the increase in its growth worldwide. Expectedly, its operations are expected to comply with the global AML/CFT measures. Ironically, the concept of Islamic banks probably because of its Islamic connotation is enshrined with feelings of negative perception. Many scholarly papers have been directed to ascertain the veracity of this negative perception. For instance, Norhashimah focused the allegation of lax control and supervision against Islamic Banking's practices in Malaysia and

²¹ Maruf Adeniyi Nasir, "Compatibility of Islamic Finance and Anti-Money Laundering Laws: A Myth or Reality?," *IIUM Law Journal* 26, no. 1 (2018): 55.

²²Finsbury Park Mosque in London, United Kingdom received a letter by its bank HSBC on the 22nd July 2015 stating the intention of the bank to withdraw services for the Mosque and the reason given was that further providing of services for the mosque is now outside its Banking risks appetite services therefore the mosque is put on notice that its account would be stand closed by 22nd of September.

²³ Maruf Adeniyi Nasir and Norhashima Mohd Yasin, "An Appraisal of Anti-Money Laundering Concept in Islamic Law," *Miyetti Quarterly Law Review* 2, no. 4 (2017): 35–66.

²⁴ IMF Working Paper, *Islamic Finance and Anti Money Laundering and Combating the Financing of Terrorism (AML/CFT)*, WP/15/XX by Nadim Kyriakos-Saad et al.

²⁵ Ibid

²⁶ Nasir, "Anti-Money Laundering Laws: The Sharia Perspectives."

Bahrain.²⁷ The study in those two countries shows that the allegation was not a true reflection of Islamic banking institutions.²⁸ It however appears that there is a need to critically examine the negative perception, its basis and veracity against Islamic in a more general form. This is because Norhashimah work was not intended to be comprehensive, although it laid foundation for a thorough work to be undertaken. Normah's article²⁹ is another study that provides an affirmative position in this regard. It traces the origin and perhaps the possible reason for the negative perception. The findings of her study are in tandem with that of Norhashimah. It confirms the existence of negative perception against Islamic financial institutions and opined that the basis for such is not restricted to Islam adherents. Normah, however concludes that various terror attacks in certain jurisdictions across the world were responsible for the negative perception. She argued that that was what is fuelling such thought.³⁰ This according to her had left some very detrimental global perceptual impacts on the Muslims and Islamic financial institutions globally. Normah opined that the consequential effect of such negative perception includes public scepticism against the Muslims and the religion of Islam. This thought is captioned as follow:

The terrorist attacks of the United States (US) World Trade Centre on September 11, 2001; Bali bombings in 2002 and 2005; London Bombing in 2005; and the Mumbai bombing in 2008 had left some very detrimental global perceptual impacts on the Muslims and Islamic financial institutions globally. As most of these attacks were carried out by some militant Islamicists, understandably there were a lot of public skepticism against the Muslims and the religion of Islam. In the United States of America (USA) for example, following the attacks on September 11, the US government enacted the USA PATRIOT Act, which is basically designed to prevent the use of the US financial system to help fund terrorism and other crimes. The enactment of the PATRIOT Act 2001 had accelerated the establishment of similar laws globally.³¹

Incidentally, the issue of negative perception against Islamic banks is tilted toward the US and its western allied. Therefore, a consistent issue, which has probably become notable feature on the negative perception of anything Islamic is that most of writings, comments or statements implicating Islamic financial institutions with terrorist financing, allegation of lax in , monitoring, control and supervision deficiencies in AML/CFT measures are either written by Western authors or the articles are perceptual in nature.³²

While Normah³³article is very much relevant as it corroborates the existence of negative perception against Islamic banks, its focus was limited to the reviews of those

²⁷ Norhashimah Mohd Yasin, "Statutory Obligations for Banks to Comply with the Anti-Money Laundering Legislation in Malaysia: Lessons from the United Kingdom," *Journal of Banking Regulation*, 2014.

²⁸ Norhashimah Mohd Yasin, "Statutory Obligations for Banks to Comply with the Anti-Money Laundering Legislation in Malaysia: Lessons from the United Kingdom," *Journal of Banking Regulation* 16, no. 4 (2015): 326–44.

²⁹ Omar, "Terrorist Financing and Perceptions on Islamic Financial Institutions."

³⁰ Omar.

³¹ Ibid

³² Ibid

³³ Ibid

few previous studies on this topic, examines related legislations, progresses to propose paper strategies on how to counter these perceptual biases and highlights preventive mechanisms adopted by the Malaysian Islamic financial institutions in mitigating and detecting terrorists financing. The article neither examined the veracity of the perception nor extends its scope outside the Malaysian approach.

Sullivan and Hendriks³⁴ did not only finger the United States of America as the major originator of this negative perception, but they equally opined that this habit is the current intolerance trend that subsist in America. In their paper titled "Public Support for Civil Liberties Pre- and Post-9/11",³⁵ they noted that whilst the American public was very intolerant of communist's socialists, and atheists in the 1950s and 1960s, the current intolerance is focused more on Muslim Americans and right-wing racists.³⁶ The current stand of former American's President Donald Trump on the recognition of the States of Israel's capital as Jerusalem despite the overwhelming condemnation and even when over 95% United Nation General Assembly members voted against such move appears to be corroborating this position.³⁷

A cursory look at the above findings will reveal that it conformed with the findings of an earlier study conducted by the Cornell University in 2004. The findings of the Cornell University clearly shown that the terror attack experienced by the Americans during the September attack had created considerable public fears in the psyche of an average Americans towards terrorism and almost half of those polled proposed that the US government should curtail civil liberties for Muslim Americans.³⁸

A careful assessment of the trend in many western countries suggests that this negative perception towards Islamic finances and Muslims is not just confined to the US. This position could be inferred from a 'Pew Global Attitudes Project' conducted in 13 countries. The countries involved in the project included the US, Spain, Britain, Germany and France. The perception as revealed by the projects shows that most respondents felt that Muslims are "violent and fanatical".³⁹

A notable development with regards to studies in this area of thoughts is that there are few studies which are not directly focused on perception of Islamic banks but have basis to proffer linkages to some perceived causes of the negative feelings. For instance, studies carried out by scholars such as. Weber in 2008 and Levitt in 2003 suggested the possibility of using non-profit organisations such 'Zakat and Sadaqah', welfare-oriented philanthropy group and financial institutions as possible conduit for terrorist financing⁴⁰.

Schneider goes a bit further in his subsequent study. His study moved from the realm of speculation to some bit of factual findings. The study linked some specific Islamic banks to some designated terrorist groups. That study shows, the Al-Shamal Islamic

³⁴ John L Sullivan and Henriët Hendriks, "Public Support for Civil Liberties Pre-and Post-9/11," *Annual Review of Law and Social Science* 5 (2009): 375–91.

³⁵ Sullivan and Hendriks.

³⁶ Ibid

³⁷ United Nations General Assembly resolution ES-10/L.22 where an [emergency session resolution](#) declaring the [status of Jerusalem](#) as Israel's capital as "null and void. In a humiliating blow for [Donald Trump](#) on the world stage, the United Nations General Assembly has voted by 128 to nine to declare his [controversial decision](#) to recognise [Jerusalem](#) as Israel's capital "null and void". See Mythili Sampathkumar, "UN Jerusalem Vote: General Assembly Rules against US, Declaring Recognition of Israel Capital 'null and Void,'" *Independent*, 2017. "

³⁸ Omar, "Terrorist Financing and Perceptions on Islamic Financial Institutions."

³⁹ PEW Global Attitude Project 2006

⁴⁰ Nasir, "Islamic Finance and Anti-Money Laundering: A Myth or Reality?"

Bank in Khartoum Sudan was sometimes used to transfer funds to various *Al-Qaeda* group companies owned by Osama bin Laden.⁴¹ In a similar vein the work of Basile in 2004 also implicated other renowned bank such as the Citibank, which he shows to have been used by the terrorist for terrorist financing activities. Basile documented how the Al-Qaeda group successfully made small financial transfers using under-regulated Islamic banking networks throughout the world to move funds from one country to another.⁴²

Assuming the above evidence linking some Islamic banks to money laundering and financing terrorism are statement of facts. Can that be enough to warrant generalisation of such view? Would it be correct to ascribe non-compliance with AML/CFT measures to Islamic banks on that basis? Would that be a sufficient justification for the alleged laxity in the supervision and control of Islamic banks?

Resolving the above questions is vital and necessary to put the issue in the right perspective. It is even more desirable if the expected complimentary role that Islamic finances is capable of rendering to the global economy is considered. Following this line of thought, this, Yazid and Nasir's⁴³ work attempted to debase such position.⁴⁴ The findings of their study show clearly that although, many Islamic banks have been found culpable, yet the number of conventional banks that have been caught for money laundering and terrorism finances related offences were substantially more compared to their Islamic counterparts.⁴⁵

A 2008 paper conducted by the Financial Action Task Force (FATF)⁴⁶ highlighted a trend by terrorism financiers of using the complex commercial arrangement of financial institutions to avoid money trail.⁴⁷ Some other writings implicating Islamic financial institutions with terrorist financing are perceptual in nature⁴⁸

An important notion is that perception represents an uncomplicated process of interpreting and organising one's thought of the meaning of a concept. However, if left uncontrolled, perception may ultimately lead to unconscious prejudice and biases.⁴⁹ Ali,

⁴¹ Konstantinos Drakos, "Terrorism-Induced Structural Shifts in Financial Risk: Airline Stocks in the Aftermath of the September 11th Terror Attacks," *European Journal of Political Economy* 20, no. 2 (2004): 435–46.

⁴² Drakos.

⁴³ Yazid Mohd Bin Kepli and Nasir Maruf Adeniyi, "Money Laundering: Analysis of Placement Methods," *International Journal of Business, Economics and Law* 11, no. 5 (2016): 32–40.

⁴⁴ Yazid Mohd Bin Kepli and Nasir Maruf Adeniyi.

⁴⁵ Nasir, "Compatibility of Islamic Finance and Anti-Money Laundering Laws: A Myth or Reality?"

⁴⁶ The FATF is an inter-governmental body which sets standards, and develops and promotes policies to combat money laundering and terrorist financing. It currently has 33 members: 31 countries and governments and two international organisations; and more than 20 observers: five FATF-style regional bodies and more than 15 other international organisations or bodies. A list of all members and observers can be found on the FATF website at http://www.fatf-gafi.org/Members_en.htm. Financial Action Task Force, "The Forty Recommendations," 2003. see also Financial Action Task Force, "Methodology for Assessing Compliance with the FATF 40 Recommendations and the FATF 9 Special Recommendations," Paris, *www.Fatf-Gafi.Org*, 2004.

⁴⁶ Jane Bourne, "Money Laundering: What Is Being Done to Combat It-A Comparative Analysis of the Laws in the United States of America, the United Kingdom and South Africa," *S. Afr. Mercantile LJ* 14 (2002): 475.

⁴⁷ Omar, "Terrorist Financing and Perceptions on Islamic Financial Institutions."

⁴⁸ Example of these are; Pieth, 2006; Drakos, K, 2004; Chen & Siems, 2004; Zagaris, 2004; and Schneider, 2010).

⁴⁹ Omar, "Terrorist Financing and Perceptions on Islamic Financial Institutions."

S.N & Syed A.R in their paper entitled "Post 9/11 Perceptions of Islamic Finance"⁵⁰ focused on three sources of data: review of mainstream media in the US, survey of Islamic finance industry professionals and an examination of Islamic finance media professionals globally. The review of US mainstream media revealed very few articles linking Islamic finance with terrorism and only 12% of the media maintained a negative tone.⁵¹

Hamin *et al* ⁵²work is equally relevant, but the coverage was equally minimal while the IMF working paper on Islamic Finance and Anti-Money Laundering and Combating Financing terrorism (AML/CFT) only laid foundation that the paper into the risk of money laundering is more required presently in Islamic banks compare to conventional bank. This conclusion can be justified if the fact that many earlier studies have been directed toward the conventional banking. Another leg from the above work is that there is need to examine other models such as level of obtainable control and compliance by Islamic Banks in a non-Muslim dominated environment like United Kingdom and where Islamic banks is the only bank in operation such as Pakistan and Iran.

When a general problem such as money laundering and terrorism financing issue is to be addressed, open mindedness that devoid a pre-conceived negative perception of any of the player appears to be a desirable approach. Thus, customer assessment risk (Risk Based Approach- RBA) would probably yield a better assessment and enforcement of AML/CFT measures. Interestingly, much effort has not been directed toward the RBA, particularly on that of Islamic banks.⁵³ Yurasina Mat Isa, *et al*, agreed with this line of reasonings and opined that the customer assessment's risk which is a major component of measuring compliance of banking institution as attracted limited studies.⁵⁴

Razzano, F.C,⁵⁵focused United States of America in his article titled America Money Laundering Statutes: The Case of a Worldwide System of Banking Compliance. He identified banks and other financial institution as the focus of money laundering legislations. The author examined United States of America existing legislations on money laundering and observed that AML laws imposed the responsibilities to detect and avoid dealings with launderers on the financial institutions in which criminal prosecution awaits any financial institutions that failed to comply.

Thus, the thrust of this work is that in the United States of America (USA), premium is placed on banks' compliance with the available AML legislations. This said to be backed up with actively and proper enforcement. In fact, all banks in the USA are mandated to have a written compliance program and its important was stressed. The focus of this work is United States of America and besides the fact that work does not touch compliance in the Islamic banking Institutions. Invariably, USA does not have basis to

⁵⁰ S Nazim Ali and Abdur Rahman Syed, "Post-9/11 Perceptions of Islamic Finance," *International Research Journal of Finance and Economics* 39 (2010): 27–39.

⁵¹ Omar, "Terrorist Financing and Perceptions on Islamic Financial Institutions."

⁵² Zaiton Hamin et al., "Configuring Criminal Proceeds in Money Laundering Cases in the UK," *Journal of Money Laundering Control* 17, no. 4 (2014): 374–84.

⁵³ Kyriakos-Saad et al., "Islamic Finance and Anti-Money Laundering and Combating the Financing of Terrorism (AML/CFT)."

⁵⁴Yusarina Mat Isa et al., "Money Laundering Risk: From the Bankers' and Regulators Perspectives," *Procedia Economics and Finance* 28, no. April (2015): 7–13.

⁵⁵ Frank C Razzano, "American Money Laundering Statutes: The Case for a Worldwide System of Banking Compliance Programs," *J. Int'l L. & Prac.* 3 (1994): 277.

make useful conclusion or conclusive comments on compliance or non-compliance of Islamic bank.

Demetis D.S,⁵⁶ identified the role of banking sector in combatting money laundering problems. He did not only observe that the crime of money laundering is on the increase, he added that only very few people has been convicted despite the intensity and continuous efforts against it globally. He contended that paper and study should be focussed on all the financial institutions. This is because, financial institutions are critical in combating money laundering related crimes.

The word all is significant. The implication of this is that banks should be addressed in the same manner and standards when dealing with issue of compliance with AML/CFT. The reason for this is that there is no major disparity in conventional and Islamic banks in term of money laundering and financing terrorism. All the financial institutions remain very crucial in anti-money laundering crusade particularly in this era of technological advancement.

A major issue addressed in Demetis⁵⁷ work is the enforceability of the AML/CFT laws. By investigating the enforcement and compliance with AML legislations in the light of the technological development, his findings show that it might not be easily enforced. No bank is immune to money laundering and financing terrorism. This is because compliance and effective implementation of money laundering laws are now faced with bigger challenges introduced by technological development.

The advent of technology advancement has broken barriers and promotes direct interaction between the buyers and customers. Thus, the AML/CFT issue has become sophisticated and limiting it to a specific bank would be erroneous. Demetis work, is therefore essentially on technological incursion in the money laundering terrain of the financial institutions.⁵⁸

Barajas, Ben Naceur, and Massara⁵⁹ contended that, much of the potential of the Islamic banking industry is yet to be exploited and presently there is no empirical evidence to suggest or confirm that Islamic banks has promoted financial access and depth once structural factors are duly accounted. López-Mejía, Aljabrin, Awad, Norat, and Song⁶⁰ raised the issue of vulnerability of banks to money laundering and concluded that the extent to which financing by Islamic banks is truly risk-sharing or whether PSIAs are fully loss absorbing, suggesting that Islamic banks may be just as exposed to risks as conventional banks. The work did not cover the issue of lax in the implementation of compliance measures by those that operates Islamic banking.

Norhashimah noted that the allegation of lax control and supervision in the implementation of AML compliance measures against Islamic banks was majorly from the United States of America, particularly from American law enforcement agencies. She posited that the contention of the US State Department, is

⁵⁶ D S DemAetis, "Technology and Anti-Money Laundering: A Risk-Based and Systems Theory Approach" (Edward Elgar, Cheltenham, 2010).

⁵⁷ DemAetis.

⁵⁸ Dionysios S. Demetis, "Fighting Money Laundering with Technology: A Case Study of Bank X in the UK," *Decision Support Systems* 105 (2018).

⁵⁹ Sami Ben Naceur, Adolfo Barajas, and Alexander Massara, "Can Islamic Banking Increase Financial Inclusion?," 2015.

⁶⁰ By Associate, Mohammad Akram, and Hafas Furqani, "NEW HORIZON Jamatul Thani - Sha ' Ban 1434 The Objective of the Shari ' Ah in Islamic Finance: Identifying the Ends and the Means," n.d., 26–31. Mr Alfred Kammer et al., *Islamic Finance: Opportunities, Challenges, and Policy Options* (International Monetary Fund, 2015).

that regulations of Islamic banks is lax control and supervision as compared to that of conventional banks.

The work emphasizes the fact that do not distinguish between complying territories and those that are not complying within countries that are operating Islamic banks. It was therefore contended cautiously that those allegations are often of a blanket nature.⁶¹ The caution exercised in the work of Norhashimah might be partly because her studies only focused on Malaysia which has been certified by FATF Styled agency Asia Pacific Group (APG) to have a comprehensive AML legislations and regulations along with reasonable compliance measures for both Islamic and conventional banks.

However, Shanmugam⁶² corroborated that of Norhashimah⁶³ on the AML compliance measures put in place by the Malaysian government. He contended that there is a well-developed AML legal and regulatory framework which includes licensing and background checks, to oversee all financial institutions in Malaysia. He therefore concluded that both the conventional and Islamic financial sectors in Malaysia are unattractive to financial criminals due to the robust regulations and the supervisory framework, which are been operating that is supported by Banks Negara (BNM)'s stringent guidelines. This is said subjected to customer identification and verification, financial record keeping, and suspicious activity reporting requirement of AML compliance measures. Besides the fact that these works of Norhashimah and Shanmugam have vehemently debunked the allegation of lax control and supervision against Islamic banks in Malaysia it is of immense⁶⁴ importance that the work is limited to Malaysia and at most Brunei.

One notorious fact that is well acknowledged by many scholars such as Norhashimah,⁶⁵ Ladan,⁶⁶ Demetis⁶⁷ and others is that money laundering technics is not static, the typologies vary and increases from time to time. It therefore becomes pertinent to constantly evaluate the compliance measures and its implementation. Thus, while it is imperative to conduct paper in the mode of operating of Islamic banks in other jurisdictions such as Iran and others, re-evaluating the present situation in Malaysia appears to be desirable in view of the complex nature of AML/CFT and positive assessment level of compliance of Malaysia with AML/CFT by the body vested with the responsibilities to formulate policy and set regulatory standards on combating money laundering, the FATF. This important because Malaysia remains one of the leading countries when it comes to the operation of Islamic banking.

⁶¹ Yasin, "Statutory Obligations for Banks to Comply with the Anti-Money Laundering Legislation in Malaysia: Lessons from the United Kingdom," 2014.

⁶² Bala Shanmugam and Haemala Thanasegaran, "Combating Money Laundering in Malaysia," *Journal of Money Laundering Control* 11, no. 4 (2008): 331–44.

⁶³ Norhashimah Mohd Yasin, *Legal Aspects of Money Laundering in Malaysia from the Common Law Perspective*.

⁶⁴ DemAetis, "Technology and Anti-Money Laundering: A Risk-Based and Systems Theory Approach."

⁶⁵ Norhashimah Mohd Yasin, *Legal Aspects of Money Laundering in Malaysia from the Common Law Perspective*.

⁶⁶ Muhammed Tawfiq Ladan, "Appraisal of Legal, Regulatory and Institutional Frameworks in Combating Money Laundering and Terrorism Financing in Nigeria," 2013.

⁶⁷ DemAetis, "Technology and Anti-Money Laundering: A Risk-Based and Systems Theory Approach."

Bourne⁶⁸ focused on the comparative Analysis of the laws in the United States of America, the United Kingdom and South Africa. The work is detail but besides the UK, the focus was not in tandem with that of the present study. The work however further exposes the UK AML/CFT regulatory framework. However, nothing shows that Muslims are culpable in non-compliance at the UK. It is of interest that despite the comprehensiveness of the UK AML/CFT laws, the defaulters in term of non-compliance by individual or corporate bodies are traced to either non-Muslims or non-Islamic organisations.

3.3. The Economic Reality

Financial system plays significant role in the economics growth of any nation because it serves as link the depositors of part of their income and the investors. The implication of this is free flow of funds within the economy along with mobilising and allocating of country scarce resources in a more beneficial manner. Financial integrity is therefore crucial. Thus, financial institutions can be said to be the most important institutional and functional vehicle that is available for the transformation of the country economy⁶⁹. Issue relating to such crucial matter ought not to be based on sentiment, phobia or any other reasons that are unfounded. Islamic banks ought to be seeing as complimentary and assessment of its compliance ought to be based on bias.

The UK is one of the highly rated country in term of strict supervision of banks, AML/CFT laws and compliance. The proof of this is the Mutual Evaluation Report (MER) on UK by the FATF. The MER reflects compliance, and the country is scored high in the core FATF Recommendations.

It is noteworthy, however that Islamic banks and conventional banks are operated in the UK and subjected to same laws and supervision. Yet the AML/CFT Mutual Evaluation Reports indicates compliance with AML/CFT regime. While many countries that operates only conventional banks such as North Korea, Cambodia, Panama, Israel, and Bahama are either blacklisted by FATF or declared to be significantly uncooperative with AML/CFT regime, Malaysia that is the hub of Islamic banks as stated earlier was not only scored high but has been admitted to membership of FATF. The MER of Malaysia reflects compliance in all the core FATF Recommendations.

Invariably, the nomenclature of banks is immaterial, as no bank is immune from being used for money laundering and financing terrorism activities. Effective monitoring, supervision, and implementation of AML/CFT laws is key and vital to secure the most needed financial integrity. Thus, in fighting a war against money laundering and financing terrorism, ensuring and promoting of a well-regulated financial systems and services is key and germane to any AML/CFT regime. Consequently, effective and comprehensive AML/CFT legislations, therefore, becomes necessary factors required in combating the AML/CFT menace. However, absence of these two will most likely incapacitate the regulatory agency even when such outcome is unintended. Consequently, to safeguard the integrity of the financial system and to guarantee legitimate business, that will not attract illegal consumers, adequacy of legislation and

⁶⁸ Jane Bourne, "Money Laundering: What Is Being Done to Combat It-A Comparative Analysis of the Laws in the United States of America, the United Kingdom and South Africa," *S. Afr. Mercantile LJ* 14 (2002): 475.

⁶⁹ Byson Beracah Majanga, "Is Time Ripe to Adopt Islamic Financial Systems in Secular Developing Countries? A Review of Literature," *Global Journal of Management And Business Research* 15, no. 8 (2015).

enforcement mechanism is germane and not whether the bank is conventional or Islamic. Interestingly, within Islamic world, Islamic finance have in the recent past become major players in the financial industries. Its significant cannot be discarded.

The world has become a global village and the two financial sectors has been perceived to be complimentary to one another, such that many non-Muslim countries are now in the fore front of adopting Islamic finance and particularly the Islamic banks. Islamic banks have therefore ceased to be in the outer realm of the global finance, it has rather occupied a mainstream. Currently, major financial institutions have open door to accommodate Islamic finances and now involving in one way or the other.⁷⁰ For instance, United Kingdom and Singapore was reported to have announced their willingness to become hubs of Islamic finance.

Several European countries have equally relaxed their laws to accommodate Islamic Finance. Countries like Australia, South Korea and France now have legislations that have become more favourable and hospitable to Islamic finances unlike what was obtainable in the recent past.⁷¹ If this spread of Islamic banks across the globe is now juxtaposed with the allegation of lax in implementing AML/CFT compliance measures, the obvious need to ascertain the veracity of that weighty allegation, assumption or statements will be desirable and necessary.

Attempt has however been made to put this in the right perspective. For instance, in a recent study, where many jurisdictions were made as case studies, it was "*found that while no financial institution is immune to laundering, the risk-sharing nature of Islamic finances poses less systemic risk than conventional finance*".⁷² The finding was that allegation of non-compliance of Islamic law with AML/CFT laws is baseless. The conclusion that can therefore be drawn is that most comments and write up about non-compliance against Islamic banks are product of perceptual error that lacks empirical evidence.

4. CLOSING

AML/CFT is a global problem and has become a renowned phenomenon. It, nevertheless, requires cooperation of all the stakeholders and countries of the world to tackle. It has caused enormous problems globally. Its risk to the international flows' volatility has becoming even more increased and foreign direct investments are adversely affected. AML//CFT risks has becoming more increased and unfortunately no financial institutions are spared from being vulnerable to this menace while its risk to the international flows is observed to be increasingly volatile. Combating this phenomenon appears to be a necessity. However, achieving success in the required global efforts to combat the menace does not only demands the cooperation of all the nations but must be rest on objectivity that devoid a preference and insinuation on personal aggrandisement. Steps that are to be taken should be all encompassing. This is because, it is obvious that no financial institution is immune from been used by the launderer. In this circumstance, the adopted approach must be all inclusive. To this end, it is the contention of this paper that rather than unnecessary labelling, castigating, or crucifying a financial sector on the ground of extraneous view, political

⁷⁰ Z Hamin, M B Othman, and S Kamaruddin, "The Evolution of the Anti-Money Laundering and Anti-Terrorism Financing (AML. ATF) Regime in Malaysia," in *International Conference on Law, Policy and Social Justice*, 2014, 10–11.

⁷¹ Hamin, Othman, and Kamaruddin.

⁷² Nasir, "Compatibility of Islamic Finance and Anti-Money Laundering Laws: A Myth or Reality?"

ideological differences or mere hatred, attention should be focused on the AML/CFT risks of all the financial institutions irrespective of their nomenclature.

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