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Evaluating the Social Control of Banking Crimes: An Examination of Anti-Money Laundering Deficiencies and Industry Success

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Evaluating the Social Control of Banking Crimes: An Examination of Anti-Money Laundering

Deficiencies and Industry Success

by

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ABSTRACT

Money laundering is a serious crime with potentially wide ranging consequences that have numerous implications for criminological research. However, criminology rarely explores this crime, nor its potential impact on other more central crimes of interest (e.g. drug trafficking or organized crime). The present study adds to a limited body of literature examining money laundering from a criminological perspective, evaluating aspects of its regulation and social control within the banking industry. Several aspects of regulatory oversight and company dynamics such as fine/settlement size, company size, and the likelihood of non-AML/OFAC violations to predict future AML/OFAC violations were evaluated. These analyses largely supported that banking crimes, and more specifically AML violations, follow the same patterns observed within previous corporate crime research. However, the primary focus of this research was to evaluate the effectiveness of industry success rankings as a form of social control as it pertains to AML violations and to determine whether or not banks that ranked well on industry rankings were also less likely to have banking violations. A variety of rankings including safety, asset-based, and overall performance measures were used to assess their relationship to bank violations, with analyses supporting that these banking industry success markers held little relationship to or acknowledgment of a firm's previous AML/OFAC violations. Implications are discussed at length including the importance of and numerous directions for future criminological research on money laundering violation within the banking industry, suggested regulatory reforms, and the need for a wider variety and more tailored industry success measures to affect some level of social control.

CHAPTER ONE:

INTRODUCTION

The present study draws criminological attention to the social control of banking crimes, and money laundering in particular. Money laundering is a significant crime, with an estimated $800 billion to $2 trillion dollars being laundered annually (United Nation Office on Drugs and Crime, 2014, Money-Laundering and Globalization). These crimes, their effects and their control, however, have largely been overlooked by criminologists.

Criminologists have long studied the idea that corporations engage in deviant activities that resemble crimes (e.g., Sutherland, 1940). Besides the absence of direct violence from banking crimes, the primary difference between corporate crimes and street crime is the form of regulation that applies: street harms are defined by criminal law whereas corporate crime are defined as social harms by non-criminal regulations, and sometimes by industry level social control mechanisms. What these behaviors share, however, is that some form of regulation identifies the behavior as a form of deviance, and that some mechanism of social control applies to these unacceptable behaviors. Thus, while the ways in which these behaviors are defined as deviant and are controlled may be different, criminologists have called attention to the fact that this difference is not really one related to the harm produced or its nature, but is a difference in how each type of harm is socially constructed (e.g., Quinney, 1970).

Corporate crimes are largely excluded from criminology because they are not socially constructed as harms by the criminal law. This does not mean, however, that those behaviors are not harmful. Banking crimes, for example, cause widespread harm and may even cause large

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scale financial disruption that can impact an entire economy. In contrast, street crime does not have this large scale impact on society. Moreover, some banking crimes such as the use of banks to launder money have been linked to the production of street crimes such as drug trafficking and to more serious crimes such as terrorism. In this sense, banking crimes may play a role in facilitating crimes indirectly.

Given the above, it is important to explore the ways in which financial regulations attempt to control banking crimes due to their direct effect on the generation of financial crises (e.g., the financial impact of the savings and loan scandal of the 1980s), and their relationship to the facilitation of some forms of street crime. One of the ways this can be accomplished is through the examination of the social control of banks. In this specific study, I do so by drawing attention to the social control of money laundering by banks.

In the present study, I lay out the ways in which banks are regulated by financial rules. One of those forms of social control involves the ranking of banks through safety, asset and overall bank performance ratings. The effectiveness of this form of social control has yet to be examined in the criminological literature. To do so, I also test a series of hypotheses relating these ratings to measure of deviant bank behavior.

As noted above, money laundering is a serious crime with potentially wide ranging consequences. One may wonder why, then, there is such a lack of concern with these crimes among the public and criminologists. Crimes that concern the general populous are typically so close to home that people are forced to believe "it could have been me". So why then should a person be concerned with money laundering? They never see it. It never appears to involve their money. How could it impact them? More difficult to explain is the lack of criminological

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interest in this topic since neglect of this issue allows criminality to continue undetected by law enforcement, encouraging future criminal activity through use of illegal proceeds, and is associated with several crimes that are of central focus in criminology today, including computer hacking, drug-related crimes, and terrorism.

The United Nations Office on Drugs and Crime estimates that between $800 billion to $2 trillion dollars (current US dollars) or 2 to 5% of global gross domestic product is laundered annually (United Nation Office on Drugs and Crime, 2014, Money-Laundering and Globalization). Laundered money funds the growth and opportunity for additional illegal acts, including the expansion of drug cartels and terrorist cells into new countries and markets, and may allow for criminal growth to occur unfettered by authorities who might otherwise combat such criminal activity.

The money laundering violations examined in this dissertation involve banks. When money laundering involves banks, it also involves violations of trust, an issue criminologists have examined as a central characteristic of corporate and white collar crimes (Coleman, 2006; Friedrichs, 2009; Shapiro, 1990). We all entrust banks with our savings. When banks launder money for criminals, billions and trillions of illegally obtained funds mingle with our money without regard for the irreparable damage this behavior may have for financial institutions.

How is this form of money laundering regulated? Banks are subject to various anti-money laundering compliance laws and regulations. They have to perform what are generally termed "Know Your Customer" (or "KYC" for short) measures on all their clientele as part of

their Client Identification Program[1] ("CIP"). These measures include extensive requirements when a customer sets up an account with the bank so that the bank can be assured that if the applicant is a person, that they are who they say they are, and if the applicant is a company, that they exist as they say they exist and only participate in the business in which they claim to be involved. Banks also have *on-going* measures that they must employ on clientele. Such measures include transactional monitoring and filing of suspicious activity reports ("SARs"). For instance, federal regulations[2] require that a SAR be filed any time that a bank, bank holding company, or subsidiary of a bank recognizes or suspects criminal violations involving insider abuse, transactions aggregating to $5,000 or more with an identifiable suspect or to $25,000 regardless of a potential suspect, as well as any time that a transaction is suspected to involve illegal or money laundering activity, or was implemented in a manner meant to evade the Banking Secrecy Act (BSA) or is outside of the normative business practices of that customer. The bank must, in those cases, research the suspicious activity to insure that the activity is not an illegal transaction or results from illegal behavior.

The regulation of banking has been complicated by the addition of regulations related to the control of terrorism. There are numerous compliance oriented regulations stemming from legislation like the Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism ("USA PATRIOT") Act of 2001, and the Currency and Foreign Transactions Reporting Act of 1970 (commonly referred to as the "Bank Secrecy Act" or "BSA"). These Acts require banks to ensure that the money passing through our banking

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[1] Please refer to 31 C.F.R. § 103.121, which is a joint regulation implementing section 3261 of the USA PATRIOT Act and requires banks, savings associations, credit unions and certain non-federally regulated banks to have a Customer Identification Program ("CIP").

[2] For further information on SAR regulations/requirements, please refer to 12 CFR 208.62, 211.5(k), 211.24(f), and 225.4(f) (Board of Governors of the Federal Reserve System); 12 CFR 353 (Federal Deposit Insurance Corporation); 12 CFR 748 (National Credit Union Administration); 12 CFR 21.11 and 12 CFR 563.180 (Office of the Comptroller of the Currency); and 31 CFR 103.18 (FincCEN).

system is *clean* money (i.e., not derived from crime), nor is money that might fund future criminal endeavors. With so many controls in place, the public may be lulled into a sense of reassurance that their banks are safe and therein, their money. What they do not take into account are two factors: (1) a law is only as good as its enforcement, and (2) even if well-enforced, there are still those who will break laws either due to ignorance of the law, or because it is beneficial to their self-interests. When it comes to anti-money laundering compliance laws, there are numerous regulations that apply to banks, some of which are very costly to enforce.

The Bank Secrecy Act (1970) was America's first and most comprehensive anti-money laundering statute. Subject to many changes over the past 40 years, it requires financial institutions to file several types of reports and to ensure that resources are available to review these reports in a time-efficient manner. The two primary filings required by the BSA are Currency Transaction Reports[3] ("CTRs'), and Suspicious Activity Reports ("SARs"). A CTR is a 2 page filing (FINCEN Form 104) that must be completed every time a cash transaction is made that totals $10,000 or more, or when a suspicious transaction involving currency occurs (typically, in a manner designed to avoid the $10,000 reporting threshold). Alternatively, a SAR is a 3 page filing that is filed for various types of suspicious transactions (inclusive of wires, insurance and loan payments/payouts, investments, etcetera). Suspicious activities that may require a SAR filing typically include any transaction indicative of insider abuses, transactions which include identifiable suspects, or are indicative of money laundering, the presence of a victim or criminal activity. The Financial Crimes Enforcement Network ("FinCEN") currently reports that a combined 15 million BSA reports are filed annually by approximately 25 million U.S. financial institutions (Financial Crimes Enforcement Network , 2014d).

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[3] For further information on Currency Transaction Reporting (CTR) requirements, please refer to 31 CFR 103.22.

The USA PATRIOT Act of 2001 imposes an even broader array of regulations on financial institutions. This Act was a reactive attempt to strengthen the existing anti-money laundering measures after finding that several reputable domestic banks, despite some 30 years of BSA regulations, had still been implicated in the laundering of money used to fund the terrorist attacks that took place on September 11, 2001. Within its hundreds of pages, the USA PATRIOT Act of 2001 contains at least 12 sections that provide new or updated regulations directly impacting financial institutions. Some are far sweeping, while others are extremely targeted. Among them, Section 313 of the USA PATRIOT Act prevents banks from having correspondent accounts for any foreign bank that does not have a physical presence in any country (this type of foreign bank is commonly referred to as a "Shell Bank"), while section 352 requires that financial institutions have an Anti-Money Laundering Program. Such a program must include a minimum of internal policies, procedures and controls; the designation of a compliance officer; an ongoing employee training program; and an independent audit function to test programs (Financial Crimes Enforcement Network , 2014b). These two sections of the Act illustrate the primary focus of the Act on defining behavior that (1) a bank *must never do* with regard to the acceptance of clientele and potential business expansion, and (2) what a bank *is constantly required to do* to be in compliance with the law.

Staying in compliance with the hundreds of regulations currently in effect world-wide can become fairly taxing on a financial institution's profit margin. Many of these requirements, while costing large sums of money to properly implement, do absolutely nothing to bring in new lines of business while imposing limitations on potential sources of new capital by restricting where and with whom a bank can do its business. It is not uncommon to find banks that have become lax on the enforcement of these compliance policies, whether due to ill-advised cost-

savings measures or in generalized ignorance of the laws and regulations. Given the breadth of anti-money laundering regulations and the potentially severe consequences of being implicated in a money laundering operation, this would be thought to be a uniquely risk-laden decision (or oversight).

However, despite having such deficiencies and being censured and/or fined as a result, banks are still seemingly quite successful within the banking industry. In fact, in 2012 Global Finance Magazine ("GF") published its "World's Best Global Banks of 2012". The *world's best banks* as of 2012 included the following institutions: Deutsche Bank, HSBC, Julius Baer, Standard Chartered Bank, Al Baraka Bank, BlackRock, BNY Mellon, Goldman Sachs, and Citi (Global Finance Magazine, 2012, World's Best Global Banks.). Among these nine industry leaders, both HSBC and Standard Chartered Bank have entered into deferred prosecution agreements ("DPAs") and paid penalties in the hundreds of millions of dollars (exceeding a billion dollars in the case of HSBC) for various anti-money laundering and sanctions violations that violate the prohibition of conducting business with countries sanctioned by the Office of Foreign Assets Control of the United States Department of the Treasury ("OFAC") (U.S. v. HSBC Bank USA, N.A. and HSBC Holdings PLC; U.S. v. Standard Chartered Bank) . Deutsche Bank is currently under investigation for conducting business with OFAC sanctioned countries (Iran and Sudan, amongst others) (Silver-Greenberg, 2012), and in the past two years, Citi has had its anti-money laundering compliance program cited by three separate regulators: the Office of the Comptroller of the Currency or "OCC", the Federal Deposit Insurance Corporation or "FDIC", and most recently, the Federal Reserve or "Fed" for consistently lacking "effective systems of governance and internal controls to adequately oversee the activities of the Banks with respect to legal, compliance, and reputational risk related to the Banks' respective

BSA/AML compliance programs" (Consent Order, US Federal Reserve System v. Citigroup Inc., March 19, 2013, pp.2-3).

It should be noted that these AML and OFAC violations do not begin to speak to the other fraud-related settlements and investigations incurred by these industry leaders. In fact, Goldman Sachs recently paid $500 million dollars to settle allegations that it sold mortgage securities to the public that it knew would fail (Securities and Exchange Commission v. Goldman, Sachs & Co, 2010). In September of 2012, BlackRock was fined £9.5 million (reduced from £13.6 million per a settlement agreement) by the Financial Services Authority ("FSA") after putting over £1.3 billion of client money "at risk" (Russell, 2012). And as recently as May 2013, the U.S. Internal Revenue Service requested that the Swiss private bank Julius Baer (Julius Baer Group AG) disclose a decade's worth of account information on its American clientele (2002-2012) in connection with the ongoing investigations of several Swiss-based financial institutions' enabling of/alleged involvement in tax evasion (Letzing, 2013).

It is becoming clear that success in the financial industry may not be greatly impacted by either allegations of or actual settlement agreements citing risk-inundated and unsavory business practices. Although such practices inherently put customers' investments in jeopardy and have the potential to support criminal enterprise, the pattern that is alluded to by some of the '*World's Best Banks of 2012*'appears to indicate that certain areas of the financial industry are routinely falling short of achieving compliance with these laws and regulations. In a world where so much is driven by financial success and so many are dependent upon their financial institutions' protection of their investments and savings, it has become important to understand why banks are taking such risks. Are the costs associated with compliance to legal requirements in this ever-changing regulatory environment so cumbersome that they largely outweigh the risks inherent in

non-compliance? What potential impact (if any) does non-compliance have on a financial institution? In a world where the financial industry's leaders are seemingly implicated in some level of unsavory business practices, and banks are becoming "too big to fail," how much does non-compliance to anti-money laundering regulation and other serious regulatory deficiencies impact industry success?

In order to investigate the issues and questions raised above, this dissertation will be organized as follows. Chapter two will provide a generalized introduction to money laundering, including a discussion of what money laundering is and the process of how it transpires including the occurrence of the underlying or 'predicate' crimes. The distinction(s) between money laundering and terrorist financing will be illustrated. Lastly, prevalence rates and examples of the detrimental impact money laundering has will be used to highlight the importance of expanding research on this issue. Chapter three will then focus on anti-money laundering efforts. Applicable laws, including the Currency and Foreign Transactions Reporting Act of 1970 ("Bank Secrecy Act" or "BSA"), the USA PATRIOT Act (2001), and the restrictions imposed by the Office of Foreign Assets Control (OFAC) will be discussed with regard to how they each attempt to limit the occurrence of money laundering. This chapter will also illustrate why banks are central to AML efforts, including the normative requirements of Banks' AML and KYC programs and a discussion of the push and pull that exists between banks and regulatory agencies where safety and expense are involved. Chapter four reviews the modest amount of criminological literature on the topic of money laundering, as well as previous research on white collar crime surrounding violations of trust as it could be applied to these types of deficiencies within the banking industry. Chapter five will comprise the data and methodology employed in this dissertation.

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Chapter six will examine how AML non-compliance impacts various types of industry success among a broader range of banks. Comprehensive data on AML, OFAC, and other serious regulatory infractions will be analyzed with rank ordered lists of industry leaders as defined by safety ratings, asset-based rankings, and overall success in an effort to reveal the true impacts of such deficiencies. Following these analyses, chapter seven will provide a discussion of the results and their potential impacts both within the banking industry and abroad as well as potential implications and future directions for criminological research.

CHAPTER TWO:

MONEY LAUNDERING IN REVIEW

A major challenge that may result from illegal activity that generates large sums of illegal income is explaining where all that money came from without implicating oneself in a criminal act. In order to avoid this outcome, money laundering becomes integral to the criminal process. Be they onetime-criminals or a burgeoning criminal enterprise, offenders who steal large sums of money must find ways to hide those resources. Hiding funds can lead to other crimes as well. The hiding of illegal funds, or money laundering, is itself a crime. In the section that follows, several intricacies of money laundering, including the process itself and various definitions, which can impact its level of legality in any given situation, will be discussed.

Predicate Crimes vs. Specified Unlawful Activities

Money Laundering is the process of converting criminal proceeds into assets that cannot be traced back to the underlying crime (Reuter & Truman, 2004). Where money laundering has been identified, the underlying crimes are referred to as *predicate crimes/offenses*. Although the International Monetary Fund (2001, p.22) identifies predicate crimes as *any* crime whose proceeds are laundered, they clarify that in most countries "only the laundering of proceeds of certain crimes is illegal". These crimes are sometimes referred to as "specified unlawful activities" or "SUAs". Although prior to the 1990s, SUAs were considerably limited and primarily focused on drugs and drug-related crimes, the list has since grown to be quite

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inclusive, including over 150 offenses as of 2004 (Reuter & Truman, 2004). The range of enforced SUAs varies across countries. One example of this variance regards tax evasion.

Though considered a predicate offense in the majority of countries, tax evasion is not considered a predicate offense within the United States. Within the USA, tax evasion's illegality is enforceable through other laws such as the BSA and the Anti-Drug Abuse Act of 1988, and it is through these other laws that tax evasion can be enforced as a form of predicate offense. For instance, in the Anti-Drug Abuse Act of 1988, a "provision was added making it illegal to evade taxes on the proceeds of unlawful activity" (Reuter & Truman, 2004, 66). This clearly speaks to tax evasion's potential use as a predicate offense to money laundering. Though it can have a harmful impact where global cooperative efforts are concerned, through tax evasion's lack of legitimate status as a listed predicate offense to money laundering, the USA also remains able to circumnavigate privacy concerns and tax law enforcement issues (Reuter & Truman, 2004).

Such differentiation exists because one of the primary purposes of anti-money laundering law has historically been to reduce the incidence of predicate crimes. As such, countries apply a targeted AML approach by addressing criminal acts that generated enough profits so that the seizure of said profits would do irreparable harm to that criminal enterprise.[4] Simply stated, some countries' AML laws provide for legally differentiating when money laundering the proceeds of certain predicate crimes is legal versus instances where that behavior is illegal. It is important to note that in both cases, the original predicate crime is illegal and therefore punishable by law; however, only in the case of an SUA is laundering those illegal proceeds also illegal.

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[4] This is why the USA does not have a need to list tax evasion as a predicate crime, as it is already covered in two other laws which would make it illegal and allow for our country's effective prosecution of it as it relates to money laundering.

The differentiation between *predicate crimes* and *specified unlawful activities* is based on cost reduction and legal function, with its application assisting a country in targeting areas where AML laws might be most effective in reducing the occurrence of money laundering and banking crimes. However, there are other typological differentiations of predicate crimes that provide more understanding of the predicate offenses as related to money laundering and the resulting policy implications of how they are treated in legal systems.

Reuter and Truman (2004), for example, divide predicate crimes into five categories based on differences in their reliance on cash, the quantity of money involved, whom the crime impacts, and the severity of the negative social impact. These five categories include: white-collar, blue-collar, drug trafficking, bribery and corruption, and lastly, terrorism. Due to the diverse natures of these predicate crime categories, each type has resulted in varying policy decisions and consequences, which may make money laundering the assets of each type of predicate crime differentially expensive and difficult to successfully complete. Some categories, such as drug trafficking, have historically drawn more scrutiny and AML regulation, resulting in vastly more difficult and costly money laundering processes.

Stages of Money Laundering

Typological differentiation is useful from an enforcement strategy perspective and indicates how difficult it may be to launder money; the general process of money laundering is typically broken up into three stages, referred to as *placement*, *layering*, and *integration*. Placement is the initial stage in the process where illegal proceeds are introduced into the financial system. This phase may include breaking down larger lump sums of cash into smaller amounts in order to directly deposit them into bank accounts, or buying high value goods (art,

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real estate, precious metals, and etc.) that will maintain their cash value upon resale. It can also involve the transportation of money across borders in order to deposit the money into foreign institutions where it may be later transferred into the US market.

The second stage of money laundering is called "layering" and involves repeated transactions that are designed to move money around utilizing various transaction types and forms of assets in order to obscure the original source of that money. Essentially, once the money has successfully made it into the financial system, layering is a technique used to mask any trail of the money's initial source, thereby concealing any previous connection it had to criminal activities or the individuals involved. Transactions commonly used in this stage of money laundering include wire transfers between accounts, account holders, institutions, or even across multiple jurisdictions, as well as the conversion of cash into alternative monetary instruments such as travelers' checks, investments in real estate, bonds, stocks, and insurance policies (typically those with early payout options), etcetera. Layering may involve as few as one transaction to multiple transactions, all depending on the amount of money involved, and the level of scrutiny to which the criminal expects the transactions to attract.

In the final stage of money laundering, "Integration", the once ill-gotten gains have been given a legitimate appearance through their re-entry into the economy as what appear to be the product of normal business practices and ventures. No longer recognizable as illegal proceeds, criminals are now free to use these assets for whatever purpose they deem worthy and with little risk of the assets being traced back to the original crime(s) that generated the funds.

Money Laundering vs. Terrorist Financing

Although the anti-money laundering efforts of the United States began with the Bank Secrecy Act (BSA) in 1970, there was a resurgence of AML attention after the attacks that took place on September 11, 2001. Shortly after these attacks, the Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism (USA PATRIOT) Act of 2001 was passed and included several new and heightened restrictions meant to derail criminal attempts to launder money. As the USA PATRIOT Act was a direct result of acts of terrorism and included heightened restrictions on money laundering that were also meant to derail terrorist activity, many often consider money laundering and terrorist financing to be one in the same. However, this is not the case as there are numerous differences between the two.

While money laundering is characterized by the attempt to conceal the criminal source of illicit funds, "terrorism financing involves the raising and processing of funds to supply terrorists with resources to carry out their attacks" (IMF, March 31, 2013). As such, the motivation for each is in stark contrast, with terrorist financing being motivated by ideology while money laundering is motivated primarily by profit. The sources are also at odds as terrorist financing can originate from numerous and often legitimate sources, including corporate, state, or individual benefactors and fundraising efforts, leading it to have a very linear monetary trail that usually involves smaller transactions below reporting thresholds. Alternatively, money laundering is sourced from criminal activity and is known to have a complex web of transactions often involving shell companies and havens, which leads to a circular monetary trail that directs the proceeds back to their initial owner.

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One important difference here is the legality of the funds' sources involved in terrorist financing. This potential legitimacy of funds involved actually limits countries' abilities to apply the existing anti-money laundering measures to terrorist financing. Recall that money laundering is meant to *ensure profits are generated from various criminal activities*, which is done through the obscuring of any connections between the crime and the funds it generated. The terrorists' funds may originate from perfectly legal sources, and rather than focusing on the generation of profits, their goal is to obtain resources to support terrorist operations. "In a number of countries, terrorist financing thus may not yet be included as a predicate offence for money laundering, and it may be impossible therefore to apply preventive and repressive measures specifically targeting this terrorist activity" (FATF, 2002, pp.9-10). It is for these reasons that, in the case of money laundering, the focus of detection is on suspicious transactions, while with terrorism financing the focus of detection remains on suspicious relationships. And, "while the phenomena differ in many ways, they often exploit the same vulnerabilities in financial systems that allow for an inappropriate level of anonymity and nontransparency in the execution of financial transactions" (IMF, March 31, 2013). As such, each poses a similar threat to the financial sector both domestically and abroad.

The Risks Implicit in Money Laundering

Once a centuries' old, well respected financial institution located in the heart of our nation's capital, in 2004 Riggs Bank was determined by FinCEN to have willfully violated the various AML requirements of the Bank Secrecy Act. Riggs Bank was investigated for several financial scandals involving money laundering. The bank allegedly held accounts of looted government money for Augusto Pinochet, a former Chilean dictator who was well known for corruption, illegal arms sales, and who had been charged with orchestrating a "wave of murders

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and disappearances that swept across the southern cone of South America in the 1970's and 1980's" (O'Brien, 2004). Riggs also held numerous accounts for Teodoro Obiang Nguema Mbasago, a dictator from Equatorial Guinea with a lengthy record of documented human rights abuses and yet, in 2004, his country was the bank's largest client. In fact, Obiang found himself a welcome lunch guest at the bank. The Federal Bureau of Investigation (FBI) also uncovered "covert" Saudi Arabian Embassy accounts at Riggs during their investigation in connection with the September 11 attacks. In 2004, Riggs Bank was fined the largest monetary penalty ever levied for such transgressions, $25 million dollars, and by May of 2005 was sold to PNC Financial Services (O'Brien, 2004). Though its AML deficiencies were egregious and clearly assisted in the prolonged ability of criminal activities to continue unabated, Riggs was not the only bank found to have been enmeshed in money laundering and, potentially, even terrorist financing. Several domestic banks were implicated during the F.B.I.'s investigations of the attacks that took place on September 11, 2001. In fact, the *National Commission on Terrorist Attacks Upon the United States* found that the hijackers "made extensive use of U.S. Banks" (Appendix A, 2004, p.138), using both "branches of major international banks like Bank of America and SunTrust, and smaller regional banks, such as Hudson United Banks and Dime Savings Bank in New Jersey."

Although the above examples are fairly egregious and well known cases, the impacts incurred in these instances do not speak to the full breadth of economic damage that money laundering is capable of creating. McDowell and Novis (2001) discuss several potential economic effects that may result from money laundering, including: undermining the legitimate private sector and the integrity of financial markets; loss of control of economic policy, economic distortion and instability; loss of revenue; risks to privatization efforts; reputation risks

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and lastly, social costs. Of these, undermining the legitimate private sector is one of the more serious effects caused by money laundering. This occurs when the front companies used by money launderers have access to substantial illicit funds, which can then be used to subsidize the legitimate front companies' business, allowing them to provide goods or services at well below market rates, and making it increasingly difficult for other legitimate businesses to compete. Financial markets can also be severely undermined when large amounts of laundered funds enter into a financial institution and are withdrawn just as swiftly and with no notice. This impacts a financial institution's liquidity and has the potential to cause runs on the banks involved. Numerous banks' failures have been connected with money laundering, including the Bank of Credit and Commerce International (BCCI), European Union Bank, and as previously detailed, the historic Riggs Bank case (Blum, Levi, Naylor, & Williams, n.d.; McDowell & Novis, 2001; O'Brien, 2004).

Not to be understated are the reputational risks and social costs associated with money laundering. With the evermore intertwined global economy, having confidence in one's bank or the country within which business is being transacted is of the utmost importance. Involvement with a place or business that has a reputation of involvement in money laundering can become a huge liability and as such is avoided by most legitimate business. After all, money laundering is a crime that allows for other criminal enterprises to expand and it literally ensures that crime does pay. To simplify, the assumption is that where money laundering is present, crime typically increases, and where crime increases, the costs of law enforcement, health care (for instance to deal with injuries and addictions resulting from criminal enterprise), and therein the costs of government all become heightened. These conditions are not symptomatic of a healthy or growing economy, and they do not generate confidence from future legitimate business

prospects. With that being said, such conditions will often increase attention from other illicit parties looking for similar services. McDowell and Novis (2001, p.8) hypothesize that "In extreme cases, it [money laundering] can lead to the virtual take-over of legitimate government." It is because of these many risks posed by money laundering that the anti-money laundering regime has enjoyed such a history of dedication and growth within the United States of America and abroad. The next chapter will briefly review some of the more significant AML laws enacted during the regime's history, as well as evaluating how effective the regime has been in its endeavor.

CHAPTER THREE:

THE HISTORY AND EFFICACY OF ANTI-MONEY LAUNDERING EFFORTS

Anti-money laundering efforts in the United States of America began in 1970 with the Bank Secrecy Act. The BSA requires banks to file Currency Transaction Reports (CTRs) on cash transactions over $10,000 to properly identify persons conducting transactions, and to keep appropriate records of financial transactions. In doing so, the BSA established the first recordkeeping requirements for all private individuals, private banks and financial institutions, while also facilitating the identification of the source, volume and movements of money transported into and out of the United States and financial institutions (Financial Crimes Enforcement Network , 2014, History of Anti-Money Laundering Laws). However, it was not until 1986 that money laundering was finally established as a federal crime under the Money Laundering Control Act. This Act also introduced civil and criminal forfeiture as potential penalties for BSA violations while simultaneously requiring banks to establish and maintain procedures to ensure and monitor compliance with the reporting and recordkeeping requirements of the BSA. As it became more difficult to use the existing bank system to launder money, criminals began to turn to other industries they could manipulate. To curb such expansion, the Anti-Drug Abuse Act of 1988 was enacted. This act expanded the application of CTR requirements by broadening the definition of a *financial institution* to include other businesses such as car dealers and real estate closing personnel and also requiring the verification of identity of purchasers of monetary instruments over $3,000.

In the 1990s, the anti-money laundering regime was bolstered by the Annunzio-Wylie Anti-Money Laundering Act (1992), the Money Laundering Suppression Act (1994), and the Money Laundering and Financial Crimes Strategy Act (1998). The Annunzio-Wylie Anti-Money Laundering Act was primarily known for its strengthening of the sanctions for BSA violations. Through the amendment of Federal law and numerous previously-existing Acts (such as the Federal Deposit Insurance Act, Federal Credit Union Act, International Banking Act of 1978, and the Right to Financial Privacy Act), it allowed for the termination of charters and insurance, as well as the removal of any party from office if the financial institution or individual was found guilty of a money laundering offense or cash transaction reporting offenses. However, the Act also increased reporting requirements through the introduction of Suspicious Activity Reports (SARs) and the addition of recordkeeping and verification requirements on wire transfers.

The Money Laundering Suppression Act (1994) was more procedurally focused, requiring banking agencies to review and enhance their training and procedures. Its amendments specifically included the development of AML examination procedures, procedures for referring cases to appropriate law enforcement agencies, and streamlining the currency transaction report exemption process.

The third Act of the 1990s that impacted the AML regime was the Money Laundering and Financial Crimes Strategy Act of 1998. This Act required that the government develop a national money laundering and related financial crimes strategy and also establish financial crime-free communities support program. Though not announced until 1999, the 1998 Strategy Act also created the High Intensity Financial Crime Area (HIFCA) program. This program was intended to concentrate law enforcement efforts at the federal, state, and local level to combat money laundering in designated high-intensity money laundering zones by creating action teams

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within each HIFCA to lead a coordinated federal, state, and local anti-money laundering effort. Currently designated HIFCAs include entire states/territories (Arizona, New York, Puerto Rico, and the U.S. Virgin Isles) but also portions of California, Chicago, Florida, and Texas (Financial Crimes Enforcement Network, 2014, What is a HIFCA?). Although HIFCAs are typically defined geographically, they can also be created to address money laundering in a specific industry sector, financial institution, or group of financial institutions (Pub. L. 105–310, Oct. 30, 1998).

Though the 1990s witnessed many amendments and improvements to the United States' AML regime, it was the events immediately following the turn the century which brought about the harshest and farthest sweeping additions to anti-money laundering legislation. In direct response to the attacks that took place on September 11, 2001, the USA PATRIOT Act of 2001 was signed into effect on October 26, 2001. This acted as a supplement to all previously existing AML laws, which, in a post-attack haze, were now viewed as vastly insufficient.

While criminalizing terrorist financing and increasing both civil and criminal penalties for money laundering, the USA PATRIOT Act was considered to be one of the most extensive anti-money laundering laws ever enacted in the United States. Title III[5] of the USA PATRIOT Act specifically targeted financial networks that were supporting criminal and/or terrorist organizations (Dolar & Shughart, 2012; Preston, 2002). The Act made it illegal to conduct business with foreign shell banks, and limited the amount of time a bank had to respond to regulatory inquiries, while also issuing several new requirements for financial institutions' ("FI") anti-money laundering programs. Included among these were: the expansion of due diligence and enhanced due diligence procedures, the mandate that financial institutions' AML training

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[5] Title III is commonly referred to as the *International Money Laundering Abatement and Financial Anti-Terrorism Act of 2001*

programs involve *all* employees whose responsibilities might require knowing the new rules (not just those employees in AML or Compliance roles), and the addition of appointing a designated Compliance Officer (also known as an Anti-Money Laundering Officer (AMLO)). In addition to the actual mandates set forth by the USA PATRIOT Act, there were also tertiary requirements, such as the apparent need to increase staff in order to comply with the now stricter and broadened CIP, due diligence, and reporting rules. Although created for the protection of many, the numerous requirements set forth in the USA PATRIOT Act had a considerably greater and potentially hindering impact on one industry over all others.

Vitality of the Banking Industry amid AML Efforts

The anti-money laundering regime is currently comprised of two parallel-running pillars: *Prevention* and *Enforcement*. Each pillar contains four key elements. Prevention includes customer due diligence, reporting, regulation and supervision, and sanctions. Enforcement includes predicate crimes, investigation, prosecution and punishment, and confiscation. Evidenced by the evolution of anti-money laundering policy and regulation over the past four decades, much of the US AML regime has focused on the Prevention pillar. As to why both have not evolved to the same extent over time, some researchers have reasoned that potential tensions exist between the two pillars. For example, discomfort or distrust of the financial supervisory authorities with the techniques employed during a criminal investigation may limit their level of cooperation with law enforcement (Reuter & Truman, 2004). Regardless, the US AML regime's targeted focus on the prevention pillar has been applied most comprehensively to '*core financial institutions*' most notably, banks.

Banks have always been a central piece to the financial infrastructure of both our country's and the global economy. Research by Monnin and Jokipii (2010) supports "banking sector stability to be an important driver of future GDP growth" (p.2). They found that periods of instability are generally followed by a decrease in real output growth (and vice versa), and that this instability would also typically be followed by increased uncertainty in potential future financial growth (p.2).

This interconnectedness was further evidenced during the financial crisis started in 2007. What originated in the United States as the result of a series of sub-prime loans being over-valued (due to the values of the housing market facing an unanticipated steep and steady decline), quickly grew to a global financial crisis. By October 2008, losses were estimated at $1,400 billion US dollars (IMF, 2008), which is also the approximate capital asset reserve of the United States. Many of these "toxic loans" were then offloaded onto European banks (Honohan, 2008). With that, many of the US and European banks involved started to face liquidity issues, and with these liquidity issues came vulnerability and distrust of other banks. In a 2009 interview with the *Observer,* Antonio Maria Costa, head of the United Nations Office on Drugs and Crime, stated that criminals exploited this vulnerability as an opportunity to launder approximately $352 billion US dollars of drug money. This significant amount of money increased the banks' liquid capital at a time of dire need, but also illustrated why the banking system, in part due to their central role in the financial sector, is at a heightened risk for involvement in money laundering.

Due to their centrality to the economy and the enhanced vulnerability this creates, many of the AML regulatory changes over time have been directed at the banking industry. The USA PATRIOT Act presented no exception to this pattern. Unlike previous regulatory changes, however, during the creation of the USA PATRIOT Act certain larger banks were invited to

provide their expertise on more robust AML Compliance programs, essentially helping to shape the requirements that would be implemented to help deter future terrorist financing and money laundering. Many of these banks were proficient in this area because they had already created and implemented these more robust AML programs. As Dolar and Shugart (2012:131) noted, "Owing to their complex organizational structures and extensive customer bases, large institutions adopted standardized AML programs long ago. Consequently, they were better equipped to comply with Title III. To the extent that regulators cooperated with large banks in designing the Patriot Act's AML provisions (and in writing the rules to enforce them), the new law provided an opportunity for large banks to impose their AML standards on the entire industry, thus gaining a significant edge over smaller competitors." Bolstering this point, Dolar and Shughart (2007) report evidence from a large national panel dataset suggesting that complying with the AML provisions of the USA PATRIOT Act has imposed a disproportionately heavier burden on smaller commercial banks and thrifts than on larger ones. Complying with the new AML regulations had an impact on banks' bottom line as well as their overall success in the financial industry. As a result, "the banking sector initially resisted increased governmental interference [. . .], but the sector has since learned how to accommodate AML requirements in ways that impose relatively modest costs and inconveniences on both banks and their customers" (Reuter &Truman, 2004, p.1).

Beyond the impact that banks can have on financial stability, the level of risk they encompass is further increased by the fact that they have historically been overly targeted by criminals as avenues for money laundering. In fact, Charles (2004) estimated that the US financial system (as a whole) houses as much as 50% of the world's money laundering activity, with 47% of the *global* total being laundered through US banks. Recent research focused on

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global banks (inclusive of US Banks) report even higher proportions of money laundering taking place via financial institutions, with specialists estimating that 50%-70% of funds being laundered annually have been laundered through global banks (Al-Qadi, Al Haj, Matar, & Hathloul, 2012). Though the estimates of illegal funds being laundered through banks represent a sizeable amount of money and therein a sizeable amount of unfettered predicate criminal activity, this does not imply that banks have played an active role in committing the laundering. The International Monetary Fund clarifies that "a financial institution can play one of three roles: (i) perpetrator, (ii) victim, or (iii) knowing or unknowing instrumentality of crime. Of these, the most common are probably when the financial institution is a victim of fraud and when it is used as an instrumentality for money laundering" (IMF, 2001, p.20). Knowing the various levels of involvement banks can play in money laundering, the frequency with which they are targeted as instruments of criminal enterprise for these purposes, and their centrality to the strength and wellbeing of financial industry, it would be reasonable to assume that research has been conducted by criminologists to not only understand, but potentially assist in creating more effective policy to future AML efforts. However, a thorough review of the available criminological literature on money laundering and the effectiveness of AML policy portray a very different reality. That literature is examined in the chapter that follows.

CHAPTER FOUR:

CRIMINOLOGICAL LITERATURE IN REVIEW

Money laundering is too often an imbedded piece of what makes large scale and organized crime prosperous. As Amanda Vanstone, the Australian Justice Minister, stated in May of 2000 during her opening remarks to the Third Annual Meeting of the Asia/Pacific Group on Money Laundering: "We need to remember that money laundered by organized crime represents the fruits of drug trafficking, arms dealing, prostitution, trade in human beings, kidnapping and extortion. Tolerating these tainted funds means tolerating the human misery that generated them in the first instance." Her statement captures the breadth of crimes touched or even enhanced by money laundering. Criminology has a wealth of research on all of these criminal activities, entire journals dedicated to drugs, organized crimes, and the like. Yet, a thorough review of criminological research evidences a distinct absence of this piece that is so central to ensuring such crimes' profitability. In fact, of the few authors who do contribute criminological research on this subject, a common thread is that all make note of is a marked lack of academic attention to the topic of money laundering. Cuéllar's (2003) research finds that "we know precious little about how the fight against money laundering really works, either in the United States, where the fight was first christened and aggressively instituted, or across the world where it has been fast adopted either in principle or practice. Nor does most scholarly work on money laundering really address this question…" (p.316). Reuter and Truman (2004) also note that in "the process of preparing [their] study revealed that there is a dearth of quantitative data

about money laundering and efforts to control it. Nor has there been much analysis of what few data exists" (p.2). Echoing that same sentiment two years later, Levi and Reuter (2006) again make note of the '*modest criminological*' literature on money laundering and the AML regime, citing the need to turn instead to nonacademic writings sourced from government, legal, and mass media journalism for information on the topic. Of the academic literature that is available, it "falls into three broad categories: (1) practical law review articles primarily directed toward identifying the necessary components of an effective AML regime and explaining the complex statutes in force to control money laundering; (2) criminological and historical analyses, many of which are highly-judgmental and value-driven; and (3) crude economic analyses of the extent of money laundering" (pp.2-3, Reuter & Truman, 2004).

Existing Literature on Money Laundering and the Effectiveness of the AML Regime

Research exploring the effectiveness of the Anti-money laundering regime finds that there are multiple goals represented by these laws and regulations. It is noted that, often, the goal is not the actual reduction of money laundering, but rather targets those criminal activities that generate these funds. Similarly, those AML laws and regulations meant to preserve the integrity of the core financial system realistically aim to achieve this goal *not* by reducing money laundering, but simply by moving it to other available channels that would have less impact on the financial system's stability (Reuter & Truman, 2004).

There have been a few studies focused on evaluating the effectiveness of the AML regime targeted on the suppression of predicate crime, and among these studies results appear to be mixed. In 2002, Levi's research indicated that the impact of AML efforts on enforcement resources, organized crime markets and drug consumption levels was only modestly understood

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at that time. Shortly thereafter, Cuéllar (2003) discussed several major failings of the AML regime including: its limited scope, disproportionate imposition of penalties towards those who are more easily detectable, relaxed and narrowly-focused regulatory authority, and global diffusion that leaves room for discretionary enforcement amongst others. In 2006, Levi & Reuter examined the overall effectiveness of the current AML regime, finding that the "Available data weakly suggest that anti-money laundering (AML) regime has not had major effects in suppressing crimes. The regime does facilitate investigation and prosecution of some criminal participants who would otherwise evade justice, but fewer than expected" (p.289). However, only three years later, Ferwerda (2009) found that stricter anti-money laundering policies, especially those inclusive of international cooperation, were associated with lower crime rates in 17 Western countries.

Over the course of three years, Reuter and Truman (2004) created two databases to evaluate the effectiveness of the AML Regime in protecting the integrity of national or international financial systems. The first included international cases reported in seven annual Financial Action Task Force (FATF) reports on money laundering typologies and in occasional reports by the Egmont Group. Of the 223 cases entered, 185 were core financial institutions (meaning exclusively banks).Their analyses of these cases revealed that 3% had been active solicitations by the bank, 3% were activities by rogue employees, and the remaining 94% included banks that were unwitting accomplices – though the authors argue it was not possible to determine if or to what extent those banks' AML controls (or deficiencies) could be accountable.

The author's (2004) second database was smaller, including only 60 cases that were ascertained from various media sources including books, newspaper articles, and the National Money Laundering Strategies. The banks' roles were identified in 55 of these cases. Of those 55

cases: 6 involved active solicitation, 4 cases involved a rogue employee, 6 were identifiable negligence via AML Control deficiencies, and 71% of cases banks proved to be unwitting accomplices. These results appear to coincide with the previous reports of the International Monetary Fund (2001), noting that financial institutions were most commonly found to be the victims of fraud or used as instrumentalities for money laundering rather than active participants in these schemes. However, it is important to note that with more than 70 percent of both samples unwittingly participating in money laundering activity, the effectiveness of AML policy is easily called into question. Although this majority of unwitting accomplices makes it easy to direct attention toward potential regulatory shortcomings, we must remember that, although the firms were labeled as 'unwitting accomplices,' more often than not they became such because of their failure to comply with some level of the existing AML policies and regulations. That level of accountability should not be underemphasized within AML research. And, as with many criminological ventures, because the data used in this research was drawn from publicized case reports, these results also cannot speak to those institutions that might be successfully navigating the AML regime without penalty.

As is well known at this point, aside from the potential for reputational damage and punitive measures, revenue brought in from potentially laundered funds are vast and enticing. As in the case of HSBC, larger banking corporations can take measures to disguise the sources of their revenue in order to circumvent AML regulations with general ease. Furthermore, the authors that have looked at the effectiveness of the AML regime repetitively call into question the level of discretionary powers embedded in current AML regulation (Levi, 2002; Cuéllar, 2003).

Although indicating potential change on the horizon, several recent achievements speak to just how much discretionary enforcement is occurring historically and at present. Among these, Senator Elizabeth Warren at her first Banking Committee Hearing (Wall Street Reform: Oversight of Financial Stability and Consumer and Investor Protections, February 14, 2013), asked a panel of senior regulators when they had last taken a big Wall Street bank to court and *none* could offer a specific example. Another example is found in a recent announcement of a policy change by the Securities Exchange Committee's new Chairwoman, Mary Jo White: That she would seek admissions of *wrongdoing* from financial firms in legal settlements. These examples support that the current AML regime does not take banks to court in the face of criminal and/or criminally negligent activities. Even in legal settlements specifying these illegal undertakings, regulators have (until recently) allowed the perpetrators to maneuver the legal system in a manner devoid of any admission of wrongdoing. It is hard to understand why such illegal activities, even once admitted and publicized, are not dealt the same breed of justice as other criminal activities. Criminology has long studied this particular type of differential treatment within the justice system, referring to it, simply, as corporate crime. In the next section, I review some of the relevant literature on corporate crime.

Definitions of Corporate Crime

In 1949[6], Edwin Sutherland presented the first definition of white-collar crime as "crime committed by a person of respectability and high social status in the course of his occupation" (p.2). In this empirical study, he examined the illegal behavior of 70 of the 200 largest financial U.S. nonfinancial corporations. Following this seminal work, initial research efforts focused on

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[6] Sutherland had earlier defined this as white-collar crime. Sutherland, Edwin H. "White-collar criminality." *American Sociological Review* 5, no. 1 (1940): 1-12, and Sutherland, Edwin H. "Is" White Collar Crime" Crime?" *American Sociological Review* (1945): 132-139

single types of offenders and offenses that would fall under this new umbrella term. Hartung (1977) examined wartime rationing violations in the Detroit meat industry, while Cressey (1953; 1970) looked embezzlers imprisoned at federal penitentiaries in order to identify specific offender types and Lane (1953; 1977) researched the role of a corporation as the offender in labor and trade violations of the New England show industry. However, many of these early authors ran into issues presented by general ambiguity within Sutherland's work. Attempting to dispel some of the ambiguity that Sutherland's work included, Clinard and Quinney (1967; 1973) argued that white-collar crime can be divided into two types: corporate crime and occupational crime. Their work defined corporate crime as illegal behaviors that are committed by employees of a corporation to benefit the corporation, company, or business. In contrast to this, occupational crime was defined as "violation of the legal codes in the course of activity in a legitimate occupation" (p.131). This differentiation further identified occupational crime as that which benefitted individual offenders for personal gain, while corporate crime benefitted organizational goals over that of any individual. The 1973 edition of this work was the first book to include a full chapter on corporate crime (chapter 8).

In 1980, Clinard and Yeager elaborated on and broadened the definition of corporate crime, stating "a corporate crime is any act committed by corporations that is punished by the state, regardless of whether it is punished under administrative, civil, or criminal law" (p.16). This more inclusive definition allowed for the study of violations of law by corporations to be considered within the same context as ordinary crime. With this, commonplace corporate violations resulting in warning letters, regulatory agencies compelling compliance, civil monetary penalties and other administratively natured enforcement actions could now be considered as violation of law by a corporation, and therein used in comparison to other ordinary

crime markers. However, as has already been discussed, the utility of such measures is called into question by the discretionary freedoms and enforcement practices currently seen within the AML regime (Levi, 2002; Cuéllar, 2003). Other punitive outlets have long been called into question for the overall effectiveness of their application to corporate crime.

One instance is Burns and Lynch's (2002) research, which called into question the utility of fines as effective deterrents for corporate malfeasance. Pointing out both the strengths and the limitations in the utility of fines, the authors cite that "criminologists have generally assumed that fines are useful mechanisms for controlling corporate behavior because they add to the costs of offending and thus are useful deterrents (Bene, 1991). Alternatively, criminologists have generally failed to explore how societal and political factors influence regulatory fining behavior" (Burns & Lynch, 2002, p.3).

Fines are argued to be a logical response to corporate crime on two fronts. The first is that corporate crimes are seen as being motivated by economic gain, and thereby effectively deterred by increasing the costs of violations though the use of fines. However, it is also highlighted that the assumptions grounding the appropriateness of fines for sanctioning corporate crime hinge on two caveats of deterrence theory; that (a) the corporations violating such regulations will be caught and penalized and (b) that the penalties assessed outweigh the benefits of the violative behaviors (Burns & Lynch, 2002).

The second rationale supporting the sanctioning of corporations by fine is one derived from potential necessity in that corporations are "organizationally diverse amalgamations of individuals acting together to achieve a specific outcome" (Burns & Lynch, 2002, p.3), and therefore when a corporation violated rules or regulations, it can be difficult to determine exactly

which individuals within that corporation are responsible. To circumvent this issue, the corporation itself may be treated as a legal entity, thereby allowing for the penalization of the corporation as a whole rather than carrying out what is often a nebulous and protracted investigation of individual contributors.

Many of the above issues discussed within the context of corporate crime can easily be applied to anti-money laundering failings, most notably those within the banking industry, with major examples previously mentioned and yet to come. However, criminological research, especially that within the confines of corporate crime, has yet to really focus on this particular financial crime.

Studies of Corporate Crime & Financial Crime

Though criminology has not focused on money laundering specifically, there have been several other related forms of financial crime that have been studied at length and lend directionality to the patterns and potential theoretical underpinnings at play. Among these related studies are several works by Calavita and Pontell (1990; 1993; 1994; Calavita, Tillman, & Pontell, 1997) examining the Savings and Loan crisis in the 1980s and Jamieson's (1994) review of Antitrust Violations.

Using the savings and loan crisis as their case study, Calavita and Pontell (1990; 1993; 1994) have explored many aspects of corporate crime. Their 1990 work highlighted the derogatory effects of ideological, political, and structural realities, finding that the structure of finance capitalism (as opposed to *industrial* capitalism which has been the predominant focus of previous white collar crime research) not only incentivizes and provides opportunities for new types of white collar crime, but also inhibits the ability of the state to respond effectively to those

new types of crime. One such structural flaw, as noted by U.S. General Accounting Office (1989), that appears as applicable to the financial industry as it has been applied to the thrift industry is the "conflicting responsibilities [of thrift regulators] for promoting the thrift industry while at the same time regulating and insuring it" (U.S. General Accounting Office, 1989, p.80). Another potential structural weakness is highlighted in the testimony of the U.S. Attorney for the Southern District of Texas before the House subcommittee on Commerce, Consumer, and Monetary Affairs (1987, p.126) where it is stated that "the public's faith in the security and integrity of their banking institutions is considered so vital to the continued viability of the banking system that Congress has promulgated laws to prevent people from even starting rumors about a bank's solvency or insolvency".

Beyond structural issues at play in corporate crime, Pontell and Calavita also draw attention to the impact of influential networks. Within the savings and loan industry there were two revolving doors: one between the state, federal regulatory agencies, and thrifts themselves, and the other involving members of Congress and members of the thrift industry (e.g. Charles Keating's campaign contributions to 5 U.S. Senators). In the case of the savings and loan crisis, the power of these networks was illustrated when in 1985, a substantial increase in both budget and enforcement personnel were "insufficient to offset the impact of political influence and favor-trading that dictated against strict enforcement" (Calavita & Pontell, 1990, p.331).

Calavita and Pontell also express, in great detail, how the deregulation ideology that took hold in the 1970s and 1980s, which was meant to promote more equitable competition under the guise that free enterprise works best when left alone, played a sizeable role in the demise of the savings and loan industry. They remark that this new finance capitalism created so much opportunity for fraud, that financial crime would really only be limited by "one's imagination".

Calavita and Pontell's (1990) focus on this deregulation highlighted a phenomenon they termed "collective embezzlement", which described the looting of one's own company for personal gain (p.321). Essentially, in this interaction between motivation and opportunity revealed how much of the fraud that took place during the savings and loan crisis was directly caused by the recently amended laws which had regulated that industry effectively until that point, and that those had been changed in direct response to developing market relations.

Calavita, Tillman, and Pontell's (1997) work adds to the body of research highlighting the state's potential impact on corporate crime. Numerous empirical findings over time have alluded that the lenient treatment of corporate offenders could be a function of the state's relationship to capital in that enforcing such regulations with any consistency would prove prohibitive of the State's other primary functions of accumulating wealth to provide stability. However, the authors highlight that many of these studies, because they were focused on manufacturing industries, focused on *social* regulations (those that are aimed at controlling production processes with goals of health and safety), while economic regulations (intended to provide stability to the economy) had not enjoyed much academic attention. Hypothetically, a structural model would predict that economic regulations should enjoy persistent and vigorous enforcement by the State which is supported by some previous research (Yeager, 1991; Shapiro, 1984). However, in the case of the Savings and Loan industry, there is "extensive evidence" to the contrary; that, not only did the state fail to prevent the crisis, but "was complicitous in shielding the thrift offenders from detection" (Calavita et al., 1997, p.32). Corporate crime involving collusion at high levels is by no means restricted to the savings and loan crisis or the thrift industry.

Jamieson (1994) reviews antitrust violations as a corporate crime that results in economic damage. Antitrust violations are essentially a set of business practices that aim to undermine competition through the collusion of competitors to establish inflated rates for their services or product, therein limiting or wholly blocking competitive pricing. Through such collusion, these former competitors are not only ensured higher profitability, but also an absence of competitors in their respective market. Numerous federal and state laws exist to curb these practices, including the Sherman Act and Clayton Act. Jamieson's (1994) research examines antitrust cases against *Fortune 500* companies between 1981 and 1985 filed by the federal government and private parties. This research examined structural aspects of the power relationships in play with corporate crime, finding that in that in a way similar to how race, income, education and occupation are used to define the social position of an individual involved with common crime, profits, size, and concentration levels are valuable descriptive factors in the characterization of organizations and corporate crime. Her research found larger corporations were more likely to be named in antitrust suits, with the most likely being large, poorly performing companies in relatively profitable industries and those with fewer managers. Jamieson speculated that poor performance when mixed with profitable industry conditions may result in a form of "turbulence that necessitates anticompetitive marketing strategies for these companies" (p.93). It was also found that the *Fortune 500* companies would lose cases to dealers and distributors less frequently, implying that the relationship of supply and demand between these prove a powerful situational manipulator.

This type of industry reliance giving way to manipulation, when applied to the financial industry, gives pause as we consider the growing oligopoly within the banking industry. Jones and Critchfield (2005) provide a thorough review of the extent of consolidation that has occurred

over time in the U.S. banking industry. Their research described the fundamental causes of this concentration trend as stemming from various environment factors such a globalization and technology, deregulation, and macroeconomic events (e.g. the attacks of September 11, 2001 or concerns over Y2K). However, they also find that, more important than knowing why this concentration has emerged is knowing its effects, both potential and realized. Although the authors do note some of the benefits of consolidation such as greater payment-system efficiency and possibly lower exposure to insolvency risk, they warn that "findings from several researchers suggest that industry consolidation and the emergence of large, complex banking organizations have probably increased systemic risk in the banking system and exacerbated the too-big-to-fail problem in banking" (Jones & Critchfield, 2005, p.42[7]).

The Federal Reserve Bank of Dallas's (2011) Annual Report strongly cautioned against allowing "Too Big To Fail" to continue, arguing that it is not only a perversion of capitalism, but that "A financial system composed of more banks—numerous enough to ensure competition but none of them big enough to put the overall economy in jeopardy—will give the United States a better chance of navigating through future financial potholes, restoring our nation's faith in market capitalism" (p.20). Similarly, Adam Davidson (2011) used data on percentages of market share from The Federal Reserve and the National Information Center to depict the evolving anti-competitive environment, citing the top three banks as holding 44 percent of the market share, with the top 20 banks collectively holding 92 percent of market share, and the remaining banks splitting what remained of the 8 percent of market share. Where so few banks hold the nation's wealth, it is easy to comprehend the risk this concentration may inherently assume, but also to envision the importance of the risks taken by the top banks to enhance their profitability.

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[7] Authors' note that "support for too-big-to-fail motive is found in Shull & Hanweck, 2001; Penas & Unal; 2004; Kane, 2000. Studies on systemic risk include DeNicola & Kwast, 2002; and Saunders & Wilson, 1999."

It would be easy to consider antitrust violations as more applicable to the manufacturing industry; however the financial industry is no stranger to this type of collusive corporate crime. In fact, though it is not related to money laundering, numerous banks were found to have participated in a similar practice involving the manipulation of benchmark interest rates. The federal government sued 17 leading investment banks in 1947, asserting that they had effectively colluded in violation of antitrust laws dating back as far as 1915. William Cohan, a former Wall Street banker turned journalist, argued for the validity of the government's case stating, "The investment-banking business was then a cartel where the biggest and most powerful firms controlled the market and then set the prices for their services, leaving customers with few viable choices for much needed capital, advice or trading counterparties. …The same argument can be made today," (2012). In fact, as recently as March of 2014, the Federal Deposit Insurance Corporation ("FDIC") sued 16 of the world's largest banks, accusing them of cheating dozens of other now defunct banks by manipulating the Libor[8] interest rate (Raymond & Viswanatha, 2014). Some of these banks have already paid billions to resolve similar charges laid by US and European authorities. Interestingly, charges based on antitrust law violation against these same banks were dismissed last March by a Federal judge after several investors sued, claiming they had lost money due to the manipulation (Raymond & Viswanatha, 2014).

A common theme that runs across these works is that certain organizational aspects of the corporate, regulatory, and political environments allow for the breakdown of policy which then lends itself to being exploited for profit. These types of theoretical underpinning are also applicable to the banking industry in relation to anti-money laundering rules and regulation in

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[8] The LIBOR is among the most common of benchmark interest rate indexes used to make adjustments to adjustable rate mortgages.

that the way the industry and its regulation is organized may be allowing for failures to continue to occur.

The penalization of banks found to have deficient AML controls have historically been anecdotally compared to a 'slap on the wrist', thus echoing the words of Gregg Barak (2012) in his discussion of the Madoff Ponzi scheme: "If financial penalties are incurred, they are a small fraction of the monies 'illegally' gotten, and none of the fined parties or corporations has to admit publicly or otherwise to any intentional misdeeds or wrongdoing. Such lawful dishonesty exemplifies the contradictions of bourgeois legality and the crimes of capitalist control alike" (Barak, 2012, p25). For AML efforts, this contradiction was recently observed within the banking industry in the case of HSBC, where federal and state authorities opted *not* to indict the London-based bank "on charges of vast and prolonged money laundering, for fear that criminal prosecution would topple the bank and, in the process, endanger the financial system. As a result of the government's investigation, HSBC has replaced almost all of its senior management, "clawed back" deferred compensation bonuses given to some of its most senior AML and compliance officers, and has agreed to partially defer bonus compensation for its most senior executives during the period of the five-year DPA" (New York Times/ December 11, 2012[9]).

Theoretical Explanations of Financial Crime

In *Class, State, and Crime (1977),* Richard Quinney argued that crimes existed because of the developing contradictions of capitalist society where those who are trying to make ends meet typically participate in crimes of a predatory or protesting nature while those people who are geared toward profit accumulation commit impersonal and/or financial crimes. In his theory,

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[9] Editorial "Too Big to Indict" http://www.nytimes.com/2012/12/12/opinion/hsbc-too-big-to-indict.html?_r=0

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crimes were both occupationally and class specific, with people's place in society determining what criminal options and/or crime control measures they might meet with. In this view, ordinary/lower class people commit street crimes which he referred to as "crimes of accommodation and resistance" making them subject to criminal law, while those in the upper class/white collar occupations participate in "crimes of domination and repression" which are more likely to be subject to civil law or regulatory controls. Stephen Box's (1983) "Integrated Theory of the Crimes of the Powerful" followed this contribution, stating that corporate crime is the result of corporations trying to achieve their goals in an uncertain environment due to economic competition, government, workers, and etc. Crime results when they resort to illegal activities while attempting to systemically reduce these uncertainties. Box's theory uses motivational strain and differential association to explain how the lack of rule enforcement of corporate misbehavior and the low risk presented by corporate punishment serve to reinforce the decision to offend (Barak, 2012).

In *The Criminal Elite (1994),* James Coleman expanded on these integrated works by explaining occupational and corporate crimes using both micro and macro level analyses. The micro level consists of motivations of the reckless and egocentric offenders while the macro level examines the structure of opportunities. Coleman argues that the origins of white collar crime can be traced to "cultures of competition" and capitalistic structures with wavering and unchecked ethical standards that are tied to profitability. Much of Coleman's theory lends itself to an argument that white collar crime becomes the product of values and practices that have been set in motion by the situational circumstances of market conditions and law enforcement. Henry Pontell's (1978; 1982) model of System Capacity also heavily weighted the enforcement of law, stating that "legal sanctioning – the celerity, certainty, and severity of punishment-

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depends, to a considerable degree, on the organizational structure of the court and also on factors external to the criminal justice system" (Pontell, 1982, p.36) This model makes the argument that sanctioning capacity is likely to be low where resources are limited and demands are heavy.

In 1989, John Braithwaite integrated structural Marxist theory (linking crime with the promotion of egoism in capitalist society) with Sutherland's differential association theory which posits that crime is learned relative to differential opportunity to create what he coined "reintegrative shaming". Braithwaite's theory makes note that there are two types of shaming: stigmatizing and reintegrative. Stigmatizing shaming has a cumulative effect in that it frequently motivates criminals to further illegal acts as they experience feelings surrounding their deviance that are increasingly negative. Reintegrative shaming, alternatively, allows the criminal to maintain their bonds with society by promoting milder forms of reprimand and shaming, followed by gestures of reacceptance.

More recently, Ke Wang's (2010) *Integrated Conceptual Model of Securities Fraud* used a multi-level integration to explain the manipulation of corporate stock prices via misleading public statements as being a function of incentivized compensation pay to top level executives. At the individual level, the theory argues that rational choice is used to evaluate risks and rewards of committing securities fraud. At the organizational level, Wang cites the importance of both constant and changing organizational attributes, in addition to the applicable corporate governance in effect. Constant organizational attributes may simply be legal entity type or location, things unlikely to change over the course of time. However, changing organizational attributes were further broken down into two groups: time varying governance attributes and time varying organizational characteristics (such as assets or competitive atmospheres in the market). The last variable included in Wang's theory is the effects of differential federal court

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decisions made on securities frauds, and how that variation may impact other's willingness to take similar risks.

Following Wang's theory, Gregg Barak put forth his *Reciprocal Model of Wall Street Fraud* in 2012, extending Wang's previous effort by incorporating three interactive models. These include Wang's *Integrated Conceptual Model of Securities Fraud*, an interactional model of organizational control fraud, and an institutional model of financial control fraud. The interactional model of organizational control fraud is a meso-level (organizational) interaction connecting control fraud, market corruption, and system capacity in an effort to understand defrauding behaviors that originate from or contained within a corporation, while the interactive model of institutional financial control fraud is a macro-level (institutional) interaction that connects financial control fraud, governing corruption, and regulatory collusion. These three models are then used to form Barak's *Reciprocal Model of Wall Street Fraud,* which stresses the roles played in the "financial crisis by the breakdown of law and the failure of governance and regulation" in allowing for corporate and Wall Street at large to avoid criminal prosecution (Galbraith, 2011; as cited in Barak, 2012).

Although Barak's (2012) theory offers one of the most recent and expansive explanations of financial crime, it is still unclear how applicable these theories may be to anti-money laundering failures in the banking industry. Many theories of financial crime focus on more clear-cut types of financial crime, for instance securities fraud. Money laundering may not fit this pattern. When members of the banking industry are implicated as having become entangled in money laundering schemes, statistics would support that a vast majority cannot be proven to have been more than *unwitting* accomplices. Many AML deficiencies are cited as being just that; failures at the corporate level to comply with current anti-money laundering regulation.

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In certain circumstances, this non-compliance can prove risky, but also potentially lucrative to a bank's bottom line. They do run the risk of allowing criminal proceeds in and therein substantial reputational risk and potential regulatory and criminal proceedings to follow, but they also conserve considerable assets thru the reductions in personnel, transactional monitoring, and overall AML program requirements they remain non-compliant with. In the current 'too-big-to-fail' era, top banks have already been bailed out by the U.S. government while regulators are continually forced to pragmatically weigh the importance of imposing stiff penalties for AML deficiencies against the paramount of ensuring the continued stability of the overall financial system. Within this atmosphere, it may be useful to gain a better understanding of just how many banking industry leaders are regular AML policy violators, and whether and to what extent the current regulatory environment has any deterrent effect on those violators given the extent of concentration of assets in the current banking oligopoly.

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CHAPTER FIVE:

DATA & METHODOLOGY

The purpose of this research is to examine anti-money laundering and compliance deficiencies with regard to how these may or may not impact banking industry success. In addition, data on banking violations will be employed to examine whether success impacts violations in the banking industry. First, various aspects of regulatory oversight and company dynamics will be examined to see if variables like fine/settlement size and swiftness, company size (both in personnel and assets), or frequency of non AML/OFAC violations predict future AML/OFAC violations. Second, the relationship between bank success ratings and violations will be examined.

The analyses will then more specifically focus on banking industry success markers; using banks' statuses on industry rankings in concert with each bank's history of AML/OFAC violations to explore how one may be related to the other and if significant relationships are found, a more in depth analysis of what may be driving this relationship will be pursued. Several types of industry success will be evaluated including safety ratings, asset-based rankings, and overall success to explore this relationship.

Data

Measures of Banking Industry Success

Three primary sources will be used to indicate success in the banking industry. Global Finance ("GF") releases three primary lists that rank banks annually. The first is GF's "World's Biggest Banks" which is typically published in October and indicates the top 50 banks world-wide ranked as measured by total assets held. Second, GF also publishes the "World's 50 Safest Banks" list[10]- which is based on an on-going comparison of banks' long-term credit ratings and total assets for the 500 largest banks around the world, and also takes into account ratings from Moody's, Standards & Poor's and Fitch's security ratings. GF has published the "World's 50 Safest Banks" list since 1996 (Global Finance Magazine, 2010). Lastly, GF also publishes the "World's Best [Global] Banks" list, that includes identifying the top banks globally in each of the following categories: corporate bank; consumer bank; private bank, emerging markets; asset management;, [global] custody; investment bank; cash management; trade finance; foreign exchange; and sub-custody.

Each of the GF lists employs numerous empirical indicators upon which the lists are built. Some of the factors included in the ranking formula, however, include some subjective measures (e.g., knowledge of local conditions and customer needs, evaluation of long-term credit ratings, effective use of technology, and profitability). Of the three GF lists, the third list is notably more subjective in its selection criteria, with selection criteria based on performance over the past year, reputation and management excellence. Global Finance's editors make their selections after holding extensive consultations with bankers, corporate financial executives and

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[10] It should be noted that the 2008 World's Safest Banks rankings only included 10 banks. All other years included the rankings of 50 financial institutions.

analysts from all over the world (Global Finance Magazine, 2010, World's Best Global Banks 2010).

Banking industry success data used in the current study ranges from 2007-2013 and are based on Global Finance's three success rankings published each year from 2008 to 2014. These rankings feature various inclusion criteria as noted above, using financial data stemming from the prior fiscal year (typically ending on December 31 of the year prior to each list's publication). These success rankings included 167 banks (i.e. *cases*) that are or have been considered industry leaders[11]. In the current study, however, additional background research was performed to account for name changes of banking firms and mergers over time which resulted in a slight reduction in cases (N =145). This issue is discussed more fully below.

Merging of Entities

The Global Finance Industry Success Rankings occasionally lacked consistency in naming conventions when referring to the same entity. In some cases this was due to name changes over the years represented within the data, while at others it was simple abbreviation usage or misspellings. Although all forms of the names used in these rankings were screened for adverse news, once those records were compiled this data was cleaned in order to have the correct entity reflected. For example, across the Global Finance data, JPMorgan Chase is referred to by four different names (J.P. Morgan, J.P. Morgan Chase, J.P. Morgan Chase & Co., and lastly, JPMorgan Chase). After all adverse news was added to these records and research was conducted, it was noted that J.P. Morgan Chase & Co. is the securities arm of the company, and thereby not considered to be a bank with most adverse news being broker/dealer securities-based

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[11] The 2014 World's Biggest Banks was never released by Global Finance Magazine and as such, World's Biggest Banks ranking and asset data is only included from 2007-2012 fiscal years.

violations cited by FINRA. As stated, the Global Finance lists denote only banks, and therefore this entity's rankings were merged with/into JPMorgan Chase. For the other three versions of the naming convention used, they are clearly three variations of the same name, two of which are differentiated only by punctuation and one which was a previous naming convention used prior to JP Morgan's acquirement of Chase. As such, all three's adverse news and industry success rankings are reflected under one entity. This approach was further supported by the consistency of rankings over time after merging the data, and the merger of data in this manner impacted approximately 16 entities and reduced the overall cases included in this research to N=145.

Measures of AML/OFAC/Regulatory Violations

As noted earlier, the measures of banking violations include AML (anti-money laundering), OFAC (Office of Foreign Assets Control of the United States Department of the Treasury), and Banking Secrecy Act (BSA) violations, which are all measures of banking regulatory violations. In this section, I examine these measures of banking regulatory violations.

There are very few indicators of a bank having deficiencies in their AML program, or involvement in illegal transactions. Research has shown that much of the banking industry involvement with money laundering may in fact be as unwitting accomplices, thereby preventing active reporting of such involvement (Reuter & Truman, 2004). As with most criminal activity, there is also a presumption that some level of this activity goes undetected, a phenomenon commonly referred to as the 'dark figure' of crime. Numerous researchers have stated this dark figure to be just as applicable to financial and corporate crime (Jamieson, 1994), as it is to other areas of criminal activity, and previous research on money laundering has followed this trend (Reuter & Truman, 2004). Also, as previously stated (see chapter one), many of those banks who

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are either actively complicit in or even just aware of such involvement are highly unlikely to publicly disclose this activity due to several factors including: the privacy inherent with client relationships in the banking industry, the threat posed by potential reputational damage in today's competitive environment, and also the regulatory and/or criminal prosecution that is sure to follow being connected with money laundering activities.

As the general public's knowledge of a bank's involvement in money laundering (whether complicit or unwitting) is generally limited by these factors, we rely on the oversight provided by regulators and investigators, who possess a direct 'line of sight' into banks' AML programs and business practices. Using their specialized knowledge of the legalities and requirements surrounding anti-money laundering efforts within the banking industry, these regulators and judicial bodies are assigned to oversee the banking industry's AML programs and, when necessary, to hold banks accountable for allowing money laundering to take place within their establishment. As such, when regulatory infractions, legal cases, or settlements concerning AML program deficiencies or money laundering are reported, these provide a uniform metric with which to gauge the level of AML program deficiency as well as the extent of money laundering that occurs within the banking industry.

BSA/AML Penalties List:

The primary measure of AML Violations was the *BSA/AML Penalties List* as reported by Bankers Online.com ("BOL"). This website provides extensive information on recent monetary penalties assessed, and C&D (cease and desist) Orders imposed by FinCEN (Financial Crimes Enforcement Network) or federal and state financial institution regulators (and others) for deficiencies in BSA/AML programs.

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On the Bankers online.com website, these cases have been arranged in reverse chronological order. The data provided for each case (when available)[12] includes: (1) the Legal Entity's ("LE's") name; (2) asset size at the time of penalty; (3), stated penalty amount; (4) agencies involved; and (5) key shortcomings noted in the organization's AML or BSA compliance program. The list also included penalties against selected individuals and non-bank organizations. The inclusion of non-bank organization illustrates that banking regulations are not only applied to banks, but rather that federal anti-money laundry law and Treasury regulations can also apply to "financial institutions" more generally. However, for the purposes of this research, only data on legal entities clearly identified as "Banks" or "Banking Financial Institutions" (i.e. Credit Unions, Banks, Savings & Loans, and etc.) have been included and analyzed. Individuals and non-bank organizations have been excluded from all analyses. After excluding individuals and non-banking institutions, the data included 60 penalties for 54 (total) banking financial institutions that had been penalized for AML/BSA violations between 01/01/2008 and 12/31/2014.

The total sample of industry success banks included 145 cases, while 54 banks were separately identified as AML/BSA violators, 6 of which were already included among the sample of 145 industry leaders while another 6 of the industry success banks had AML violations stemming from sanctions imposed by other countries (captured through the World Check screenings). Thus, among the sample of 145 banks, a total of 8.2 % (N = 12) had an AML/BSA violation. The AML/BSA data was used primarily for RQ2/Hypothesis 2 because it was the only source that regularly recorded assets at the time of AML penalty, and then the same

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[12] All data was available with the exception of Assets at the time of penalty (Available in 53 of the 60 cases/penalties samples)

data was also used as a double check the AML/Sanctions data pulled for all the Industry Success Banks (which originated primarily from World Check screenings).

OFAC Sanctions

The primary source measure for OFAC sanctions is provided by The U.S. Department of the Treasury's Resource Center's "Civil Penalties and Enforcement Information" (U.S. Department of the Treasury, 2014, Civil Penalties and Enforcement Information). Within this Information Center, OFAC Sanction and Settlement information is provided dating back to 2003 in the form of .pdf documents. Each OFAC PDF "Enforcement Information" document contains major points of the case as provided by the Treasury Department in its investigation of the target. This information includes: (1) a brief explanations of the violations; (2), the sanctions being imposed and (3) the monetary penalties associated with the sanction. The initial results page for each year (ranging from April 2008-2013) was saved, and all OFAC enforcement actions were then sorted and saved according to Bank versus Non-Bank status. Non-banks filings were retained for record-keeping and potential future use, but were not included for use within this study. All bank-related Enforcement Information documents were reconciled with, and then added to any OFAC data pulled from the World Check adverse news screenings.[13]

Regulatory Violations (Inclusive of AML and OFAC):

Thomson Reuters Accelus' "World-Check" Screening service was used as the primary source for identifying varied regulatory violations, as well as a general supplement for AML violation and OFAC sanctions information. World-Check is a well-known risk analysis service provided by Thomson Reuters Accelus that was created to provide the financial industry with a

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[13] World Check adverse news profiles also included OFAC Investigations, which were counted separately.

meticulously collected, thorough, and current list of all regulatory, AML, and OFAC violations against screened targets. This service is typically used to provide an overall illustration of the risk inherent in doing business with a target entity or individual.

For this research, all banks referenced on the various indices of bank "Industry Success" (as described earlier), were screened thru World Check and any adverse news reported for each bank was recorded, coded and added to the dataset. Each screening produces a results page, containing links to the profile pages of any potential matches to the screened name. If the screening target had an identifiable profile as a result, that profile page's link was accessed. This brings the user to that Legal Entity's *Profile Page,* which is unique to that entity and coded by the Profile "UID" noted at the bottom center of each page. Any adverse news contained within this profile page's "Biography", "Identification" and/or "Reports" categories were recorded and coded for analysis. Adverse news findings, regardless of their nature (regulatory, OFAC, AML, etc.), are all dated with both month and year. Each news article typically provides a summary statement of each finding, with source documents accessible in provided links. All adverse news information was chronologically sorted and added to the dataset. Please see Appendix B for further information on the World Check data collection and cleaning process.

The World Check screening service allows for systematic screening of the industry leaders based on the legal entity's name presented in the Global Finance rankings and provided a complete and thorough depiction of all adverse news regardless of time frame. The other two data sources will ensure the inclusion of banks that potentially do not rank as an industry leader, but have severe AML and/or OFAC violations. While World Check screenings provide all adverse news available based on the entity name screened, data from BSA/AML Penalties list and from The U.S. Department of the Treasury's Resource Center's "Civil Penalties and

Enforcement Information" were only collected for years 2008-2013 in an attempt to match the industry success data's time frame but also due to data limitations. Please see Table 1below, for a consolidated depiction of the variables that will be used in this research.

Table 1: Variables Included in Study		
Variable Name	Variable Summary	Variable Source
Measures of Banking Industry Success		
World's Biggest Banks	Based on total assets held	Global Finance Magazine's World's Biggest Banks
World's 50 Safest Banks	Based on an on-going comparison of long-term credit ratings in concert with total assets of the 500 largest banks in the world	Global Finance Magazine's World's 50 Safest Banks
World's Best [Global] Banks	The top bank in the world a number of categories based on selection criteria including: performance over prior year, reputation, & management excellence	Global Finance Magazine's World's Best [Global] Banks
Measure of AML/OFAC/Regulatory Violations		
BSA/AML Penalties List	Recent monetary penalties assessed and C&D Orders imposed by FinCEN or federal and state financial institution regulators (and others) for deficiencies in BSA/AML programs	BankersOnline.com
OFAC Sanctions	OFAC Sanction and Settlement information	The U.S. Department of the Treasury's Resource Center's "Civil Penalties and Enforcement Information"
Regulatory Violations (Inclusive of AML & OFAC)	Current list of all regulatory, AML, and OFAC violations against screened targets	Thomson Reuters Accelus' "World-Check" Screening service

Methodology

There are four primary data sources used to indicate success in the banking industry and three sources measuring AML, OFAC, and serious regulatory deficiencies. Data collected will reflect a 7 year time frame with regard to AML, OFAC and regulatory violations (2008-2014), as well as banking industry success. The Industry ranking data released from 2008-2014, with the exception of 2014's Biggest Banks, resulted in approximately 170 banks (i.e. *cases*) that are or have been considered industry leaders. As previously discussed, this number was subject to background research so as to account for name changes and mergers. Correcting for names changes and mergers, the final sample size was reduced to 145 cases.

Chapter six examines how AML non-compliance impacts various types of industry success among a broader range of banks. Comprehensive data on AML, OFAC, and other serious regulatory infractions will be analyzed with rank ordered lists of industry leaders as defined by safety ratings, asset-based rankings, and overall success in an effort to reveal the true impacts of such deficiencies. Several hypotheses can be generated to test various relationships suggested above.

Hypotheses and Research Questions

Research Question 1 - Can AML violations be used as an indicator of more entrenched regulatory disregard/corporate malfeasance among banks?

This research questions gives rise to the following hypothesis:

H₁ – Banks having AML and/or OFAC related violations will have significantly more regulatory infractions of a non-AML nature than those banks with no AML/OFAC violations in their profile.

Prior research has suggested that corporations possessing a history of violations may be prone to committing other types of violations. In prior studies, this relationship indicates that organizations with known patterns of wrongdoing may include a supporting culture that reinforces illegal activity and therein may be likely to result in further violations (Baucas & Near, 1991; Clinard & Yeager, 1980; Finny & Lesieur, 1982). In other words, banks with AML or OFAC violations may have "criminal cultures" that lead to violations of other forms of regulations related to banking. As money laundering and OFAC violations are among the most damaging violations a bank can receive (due to regulatory emphasis as well as public scrutiny), they are hypothesized to be more likely possess a culture which promotes regulatory violations. Thus, banks with AML/OFAC violations are hypothesizes to be more likely to have non-AML/OFAC violations as well.

Research Question 2 - Prior research on corporate crime has suggested that fines for corporate crime are not very large. Those fines may appear large in the aggregate, but relative to a corporation's assets, those fines tend to be small. To examine whether this conclusion applies to money-laundering offenses within the banking industry, a table showing the distribution of fines as a percentage of corporate assets will be created.

Barnett's (1981:5) research offers a simplified economic explanation for understanding corporate crime, stating that "one can expect that a corporation will be relatively likely to choose to engage in crime when the expected costs of its illegal action are acceptably low relative to

perceived gains." Following Barak's (2012:25) assertion that "if financial penalties are incurred, they are typically a small fraction of the monies 'illegally' gotten'", it can be argued that when applied to the banking industry there may be a cost-based incentive to continue operations when AML or OFAC penalties are small. We know that, at least in certain cases (e.g.: HSBC), there are banks willing to take illegal risks. What is unknown, however, is whether fines meted out under regulatory responses are "large enough" to deter future criminal behavior.   At issue, then, is whether the current level of fine are, in fact, stringent enough to act as a deterrent, or as Barak stated, merely a 'slap on the wrist'? Assessing the relationship between fines meted out and bank assets is one way to address whether fines appear sufficient to deter future offending. Based on these observations hypothesis 2 proposes:

> H_2 – There will be no statistically significant difference between violations before
> and after a fine is imposed, indicating fines have little to no impact on earnings.

As Barak (2012) argued relevant to Madoff's Ponzi scheme and Wall Street more generally, small fine sizes are expected relative to total company assets, and with this disparity, it is also expected that such regulatory fines and settlements should have little to no impact on the overall earnings of the bank(s).

Research Question 3 - Does size of corporate entity predict likelihood of AML violation?

> H_3 – Based on the Dalton and Kesner's (1988) research, it is expected that the size of a
> bank will impact the likelihood of regulatory infractions.

This general hypothesis gives rise to two more specific hypotheses (H-3-A and H-3-B) that can be empirically assessed.

H$_3$a- There will be a positive correlation between employee numbers and regulatory infractions. As such, the larger the bank is (based on total personnel), the more regulatory infractions are expected to be found.

H$_3$b – If a strong positive correlation coefficient is found between total personnel and regulatory infractions, then size of the institution based on total assets will also predict violation(s).

Clinard and Yeager (1980:44) stated the importance of structure of organizations in predicting corporate crime early on, noting that "these factors – size, delegation, and specialization –combine to produce an organizational climate that allows the abdication of a degree of personal responsibility for almost every type of decision, from the most inconsequential to one that may have a great impact on the lives of thousands." Focusing more closely on size dynamics, Dalton and Kesner's (1988) researched how company size impacted illegal activity. They discovered that "large" firms within their sample were approximately three times more likely to engage in illegal behavior than the smaller companies, and that recidivism in the form of multiple violations was also three times more likely among those larger companies. Based on this line of research, the size of the bank is similarly expected to impact the likelihood of AML/OFAC regulatory infractions, as well as recidivism.

Research Question 4 – Do AML Violations Impact Industry Success?

Theoretically, one would expect that banks that receive high quality ratings would be less likely to have engaged in regulatory violations. This gives rise to the following hypothesis.

H$_4$– The rankings of banks listed on the "Best" list will be negatively correlated with the presence of AML and/or OFAC fines/citations/sanctions.

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This relationship can be assessed by examining the correlation between the "World's Best Banks" rating and violations. The selection criteria for Global Finances' World's Best Banks' winners included performance over the past year, reputation and management excellence, and other subjective qualifiers. Based on the reputational damage that accompanies money laundering violations can generate, in concert with the notion that management excellence is exemplified through a record of avoiding fines, infractions, and other serious violations of laws and banking regulations, we would expect that banks listed on this "Best" list have had relatively little to no involvement in such infractions.

While "Best" banks may have better regulatory records, hypothesis 3 suggested that the likelihood of infractions may also be the result of an entity's size. In hypothesis 3, size was assessed using measures of personnel and assets independently. Here, we introduce an alternative measure of size taken from the list of "Biggest Banks." Using that list, hypothesis 5 suggests:

H_5– The rankings of banks listed on the "Biggest" list will be positively correlated with the presence of AML and/or OFAC fines/citations/sanctions.

As suggested by Dalton and Kesner's (1981), Barnett's (1981) and Barak's (2012) research on the impact of size dynamics on illegal activity suggest, large banks may be more likely to be involved in regulatory violations. In this hypothesis, it is expected that the those banks listed on the "Biggest" 50 banks ranking will have increased involvement in AML/OFAC fines, sanctions and settlements.

Hypotheses 3, 4 and 5 address some of the potential correlates of banking regulation violations. In addition, one might expect that banks ranked as "safe" might be less prone to regulatory violations. This leads to hypothesis 6 which suggests:

H_6 - The rankings of banks listed on the "Safest" lists will be negatively correlated with the presence of AML and/or OFAC fines/citations/sanctions.

To assess this relationship, Global Finance Magazine's rating of the safest banks was used. Global Finance Magazine's "Safest" banks ranking was created through an evaluation of long-term credit ratings and total assets of the 500 largest banks worldwide. Although assets were previously hypothesized to be positively correlated with AML and/or OFAC violations, when they are taken in concert with long term credit ratings, this relationship is hypothesized to revert back to a negative correlation. Long term credit ratings provide a much higher level of scrutiny of a bank's financial profile by examining the credit risk of each institution in order to examine the likelihood of them being able to fulfill financial obligations over time. Were a bank found to be complicit in money laundering, or even merely deficient in AML controls, the fines, sanctions, and/or settlements they would face, in addition to the business they may lose (either due to reputational damage or regulatory intervention) and expense necessary to bring their AML program to code, would presumably have a grievous impact on their risk profile, thus lowering their overall safety ranking. Thus, one would expect that there would be a negative correlation between GF's safety rating and regulatory violations among banks.

Proposed Analyses

Several of these hypotheses can be addressed through the use of Pearson Correlations. For instance, all three hypotheses exploring the relationship between banks' industry ranking and

their AML/OFAC violation history will be initially assessed in this manner. Additionally, Pearson correlations will also be used to examine whether the size of a bank plays a role in the occurrence of AML/OFAC violations by exploring whether increases to the number of total personnel in a company also increases the likelihood that corporate malfeasance as it pertains to AML/OFAC violations. Lastly, for those remaining hypotheses that require more stringent statistical analyses which assume variables are related, Pearson correlations will first be employed to ensure this relationship is statistically significant. If the relationships' significance is supported, then a series of both linear and logistic regression models will be employed to further evaluate the existing relationships. Where AML/OFAC violations are the outcome variable, logistic regression will be used due to the dichotomous nature of this variable. For instance, in the event the there is a significant correlation found between ranking as one of the *Top 50 Safest Banks* is found to be significantly related to the AML/OFAC violation variable, we would predict that the higher the rank on this success indices, the less likely there is any AML or OFAC violation present against that company. Alternatively, analyses testing asset-based hypotheses or involving other continuous variables (i.e. personnel totals, fine/settlement amounts, and etc.) will employ the most appropriate linear regression model for the variables included.

CHAPTER SIX:

ANALYSES

This chapter presents the data analysis related to the four research questions and eight hypotheses (including H1-A and H1-B) specified in the previous chapter. The sections below present the analysis by the specific research question and hypotheses addressed.

Findings: Research Question 1, Hypothesis 1

In order to examine whether AML violations can be used as an indicator of more entrenched regulatory disregard/corporate malfeasance, the number of adverse news findings reported by each entity's World Check screening process was recorded and segregated into four separate variables: (1) AML findings; (2) OFAC sanctions; (3), non-OFAC/sanction related findings; and (4) General Adverse News (i.e. regulatory findings not including AML of OFAC related violations). Quantifying non AML/OFAC adverse news findings in this manner resulted in each entity having a violations count for each type of specified adverse news event ranging from 0, meaning no adverse news was reported (N=71 out of 143[14]) to 19 reported violations (N=1). This distribution is illustrated further in Figure 1.

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[14] Data for two banks from the original sample was unavailable, reducing the sample for this portion of the analysis to 143 cases.
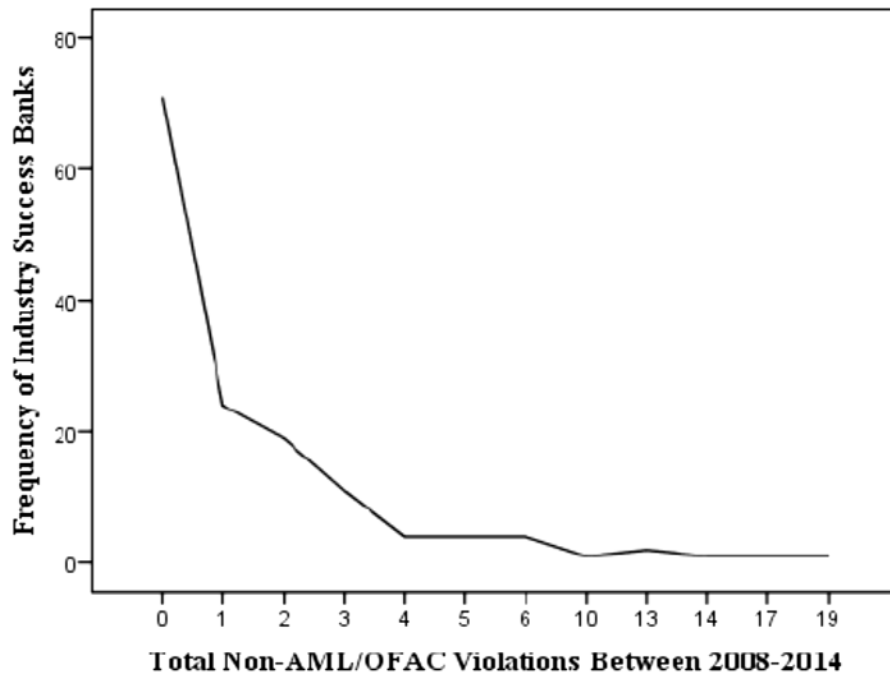
Figure 1: Distribution of Non-AML/OFAC Violations Across Sampled "Industry Success" Banks

Table 2 shows the distribution of non-AML/OFAC infractions for banks with and without AML/OFAC infractions. The table suggests that, while approximately half of the total banks sampled as Industry Leaders had some form of non-AML/OFAC violation, nearly a third of those banks with non-AML/OFAC infractions also possessed AML/OFAC violations. Further analyses found below tests whether this distribution is statistically significant.

Table 2
Association Between AML/OFAC Infractions and Non-AML/OFAC Infractions (N=143)

Banks with Non-AML/OFAC Infractions	72 (50.3%)
Banks with AML/OFAC Infractions	22 (30.6%)
Banks without AML/OFAC Infractions	50 (69.4%)

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For the remaining three categories (AML; OFAC sanctions; and Non-OFAC/Sanctions) the data were then merged into a dummy variable whereby the presence of a violation in any of the three was coded as a 1 (violation present) or 0 (absent; no violation).[15] Due to the dichotomous nature of the dependent variable and the interval nature of the non AML/OFAC adverse news count variable, a binary logistic regression was estimated to explore whether increased adverse news violations would predict the presence of AML/OFAC violations. This logistic regression model was significant (-2LL=123.21, $\chi^2_{(1)}$ =18.23, p<.001), while also indicating that it held poor predictive power (Nagelkerke R_2 =.191). The model supported hypothesis 1 - that Non-AML/OFAC Adverse news has a significant effect on the likelihood of AML/OFAC violations (b = .285, p=.001). The results indicate that a one unit increase in adverse news produces a 0.29 increase in the odds ratio of the bank possessing an AML or OFAC related violation. These results indicate support for hypothesis 1; that is, banks having a higher number of regulatory infractions of a non-AML nature will have a significantly higher likelihood of possessing an AML and/or OFAC related violation than those banks with little to no regulatory infraction history. This result suggests that the presence of AML/OFAC violations can likely be used as an indicator of more entrenched regulatory malfeasance.

Findings: Research Question 2, Hypothesis 2

Prior research on corporate crime has suggested that fines for corporate crime are not very large. Those fines may appear large in the aggregate, but relative to a corporation's assets, those fines tend to be small. To examine whether this conclusion applies to money-laundering

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[15] A precursory bivariate correlation was conducted between the number of non-AML/OFAC violations and the presence of AML/OFAC violation to ensure a significant relationship existed to warrant further examination, and evidenced a significant moderate relationship (r =.395, P<001).

offenses within the banking industry, Table 3 depicts the distribution of fines as a percentage of

corporate assets at the time of penalty.

Table 3: Distribution of AML Fines and FI Assets at Time of Penalty   (N = 54)

Date of Penalty	Financial Institution ("FI")	Monetary Penalty Imposed (US/$)*	Assets Held by FI	% of Assets
11/25/2014	North Dade Community Development Federal CU	300 K	4 M	7.5
6/26/2014	Associated Bank, N.A.	500 K	24.5 B	0.002
1/14/2014	Old National Bank	500 K	9.5 B	0.005
1/7/2014	JPMorgan Chase Bank (et als)	2.05 B*	2.5 T**	0.08
9/24/2013	Saddle River Valley Bank	8.2 M *	10 M	82
9/23/2013	TD Bank, N.A.	52.5M	212B	0.03
6/28/2013	North Dade Community Development Federal CU	C&D	5.8M	0
6/17/2013	M&T Bank Corporation	Written Agreement	83B**	0
1/25/2013	TCF National Bank	10 M	17.9B	0.06
12/10/2012	HSBC Holdings Plc	1.9 B	N/R	N/R
11/16/2012	First Bank of Delaware	15M / "Death Penalty"	222.5M	6.74
4/4/2012	Citibank, N.A.	C&D	1,288 B	0
8/22/2011	Ocean Bank, Miami, FL	10.9 M	3.6 B	0.3
3/23/2011	Pacific National Bank, Miami, FL	7 M	358 M	1.96
2/11/2011	Zions First National Bank,	8 M	17B	0.05
1/31/2011	Mizrahi Tefahot Bank, Ltd.	350 K	1.3 B	0.03
9/1/2010	First National Community Bank	C&D	1.3 B	0
8/26/2010	Ozark Heritage Bank, N.A.	C&D	66.2 M	0
7/20/2010	TCF National Bank	C&D	18 B	0
6/21/2010	Intercredit Bank, NA	200K	267.3 M	0.08
5/19/2010	Security Bank, N.A.	C&D	148.2 M	0
10/7/2010	HSBC North America Holdings, Inc. & HSBC Bank USA, N.A.	C&D	N/R	N/R
5/10/2010	[Former] ABN AMRO Bank N.V.	500 M	N/R	N/R
4/22/2010	Eurobank, San Juan, PR	25 K	2.56 B	0.001
3/29/2010	Pamrapo Savings Bank, SLA,	6M*	559 M	1.07
3/12/2010	Wachovia Bank, N.A.,	160M*	510 B	0.03
10/26/2009	Family Bank and Trust Co.	800K	78 M	1.03
8/5/2009	First Standard Bank	C&D	139 M	0

Table 3 (Continued): Distribution of AML Fines and FI Assets at Time of Penalty

Date of Penalty	Financial Institution ("FI")	Monetary Penalty Imposed (US/$)*	Assets Held by FI	% of Assets
8/4/2009	Heritage Bank of North Florida	C&D	194 M	0
4/2/2009	Rocky Mountain Bank & Trust Florence	C&D	200.6 M	0
4/20/2009	Doha Bank New York Branch	C&D	N/R	0
2/24/2009	Bank of Westminster	C&D	29.7M	0
2/12/2009	Upstate National Bank	C&D	96.5M	0
2/12/2009	University Bank	C&D	129.3M	0
1/29/2009	First Vietnamese American Bank	C&D	53M	0
12/3/2008	West Suburban Bank	C&D	1.85 B	0
11/13/2008	Mountain Commerce Bank	C&D	345.1 M	0
11/7/2008	Dresdner Bank AG	C&D	N/R	0
11/3/2008	Blue Ridge Savings Bank, Inc.	C&D	298.4 M	0
10/27/2008	Polk County Bank	C&D	163 M	0
10/24/2008	Eastern National Bank	200 K	479 M	0.04
10/17/2008	Fort Davis State Bank	C&D	58.7 M	0
10/16/2008	Sanderson State Bank	C&D	38.2 M	0
10/7/2008	Omni National Bank	C&D	1.03 B	0
10/2/2008	Kenney Bank and Trust	C&D	59 M	0
10/2/2008	The Bank of Harlan	C&D	126.6 M	0
9/25/2008	First Asian Bank	C&D	39 M	0
9/15/2008	Citizens Community Bank	C&D	46 M	0
9/9/2008	Intercredit Bank, N.A.	C&D	373 M	0
8/27/2008	Mizrahi Tefahot Bank, Ltd.	C&D	282 M	0
8/21/2008	Chestatee State Bank	C&D	286 M	0
7/9/2008	T Bank, N.A.	C&D	152M	0
6/4/2008	Eastern National Bank	C&D	476 M	0
4/30/2008	Sun Security Bank	C&D	440 M	0
4/22/2008	United Bank for Africa, PLC	15 M	441 M	3.4
3/14/2008	Independence Bank	C&D	383 M	0
3/10/2008	First Regional Bank	C&D	2.17 B	0
2/29/2008	United Bank for Africa, PLC	C&D	N/R	N/R
2/26/2008	Wallis State Bank	C&D	274 M	0
2/19/2008	Doral Bank	C&D	7.7 B	0

C&D = Cease & Desist Order (No Fine), K = Thousand, M = Million, B = Billion, T = Trillion, N/R = Not Reported
* Denotes multiple financial penalties have been summed, ** Denoted Holding Company Assets

As presented in Table 2 above, the penalties levied against banks for BSA and AML violations often reflected only a small fraction of the assets held by the financial institution at the time of penalization. Table 4 provides further analysis of these fines.

Table 4	
Descriptive Statistics of AML/BSA Penalties (2008-2014; N=60)	
Number Fined Firms	54
Number of AML/BSA Penalties	60
Total Monetary Fines Levied	21
Total Non-Monetary Fines Levied	39
Average Monetary Fine/Event with Fine	$225,975,000
Average Monetary Fine/All Events	$87,879,166
Total Firm Assets	$4,708,290,100,000
Average Firm Assets	$88,835,662,264
Average Fine as % of Firm Assets	1.77
Range of Fines	$25,000 - $2,050,000,000

Please Note: Firm assets at time of Penalty were provided in N=53 of the 60 cases.

For example, for the 21 cases where there was a monetary penalty, the penalty ranged from $25,000 to $2.05 billion, or between 0.001% to 7.5% of a bank's assets. In addition, of the 54 banks penalized, only 38.9% received a monetary penalty. The mean penalty for the 21 banks assessed a financial penalty was $225,975,000. Across all 54 banks, the monetary penalty was substantially lower, $87,879,166. Only 6 banks received a financial penalty greater than 1% of their assets. Eight of the financial penalties were for more than 1 million dollars, and those fines began with the smallest million dollar fine of $ 7 million against Pacific National Bank. These fines, as noted, were generally a small percentage of a bank's assets. Even in the case of JP Morgan Chase where a fine of $ 2.05 billion dollars was imposed, the fine was only 0.08% of

bank assets. Thus, it would appear from these data that the handful of fines received by banks appear "large" in that they impose millions in fines. Yet, in relative terms, the fines are small compared to bank assets.

Although the distribution of fines noted above does support their fairly inconsequential size relative to assets held, this does not speak to the potential impact of these fines on the well-being or future success of the financial institution. A review of the current state of this sample shows that, of the 60 AML/BSA penalties noted above on a total of 54 financial institutions, 14 banks have since either failed (N=13) or received a regulatory "death penalty" (N=1), while another 7 have subsequently merged with other banks and in essence no longer exist independently as they did when penalized. This would indicate that slightly more than 25 percent of banks penalized within this sample did not survive 6 years after being cited for an AML/BSA violation. However, this does not necessarily speak to the impact of the actual penalty imposed. In point of fact, only 4 of the failed banks and 3 of the subsequently merged banks were subject to any monetary penalty due to their violation(s) (rather than Cease & Desist Orders).

Assets held at the time of penalization were compared to current total assets as reported on December 31, 2014 (sourced primarily from FDIC via USBankLocations.com[16]) through the use of a paired sample t-test. The results supported hypothesis two, that there is no statistically significant difference between before violation and after violation earnings, further indicating that fines typically have no impact on earnings ($t_{(51)}= 1.280$, $p>.05$). Thus fines do not appear to have any reputational impact that causes customers to avoid banks with violations. This, in combination with the knowledge that over 25 percent of banks cited in the sampled AML/BSA violations have not survived independently to date, may support the impact of other aspects of

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[16] http://www.usbanklocations.com/bank-rank/total-assets.html

AML/BSA violations such as reputational damages incurred by the institution or the costs of correcting AML/BSA program shortcomings, rather than any direct impact incurred though the monetary penalties imposed.

Findings: Research Question 3, Hypotheses H3, H3-A and H3-B

In order to investigate whether the size of a corporate entity predicts the likelihood of an AML violation taking place (hypothesis H-3), the relationship between corporate size and violations was assessed using two sub-hypotheses, H-3-Aand H-3-B. Hypothesis H-3-A predicted the relationship should be between size of a bank measured by number of personnel, while H-3-B measured that outcome using corporate assets as the size measure.

For hypothesis H-3-A, the size of each bank within the sample was indicated by the total personnel as reported through recent annual reports or company web pages. Total personnel numbers were then compared to the count of non-AML/OFAC adverse news through a Pearson correlation. As predicted by hypothesis H-3-A, a significant, though weak, positive correlation was found ($r=.228$, $p<.05$) supporting Dalton and Kesner's (1988) research which suggests that as the size of a bank may impact the likelihood of regulatory infractions with the regulatory infractions (based on total personnel) increasing with size of bank. Total employee counts and total non-AML/OFAC violation counts are significantly correlated in the expected direction.

With respect to hypothesis H-3-B, a second series of Pearson correlations was estimated to examine if there was a correlation between violations and assets (as indicated by assets reflected for those ranked "Biggest" Banks). The correlation between total assets and the count of total non-AML/OFAC violations was moderate for 5 of the 6 individual years examined

(2008-2012: r= .426, .454, .412, .433, .427, p<.01), with the remaining year (2013) holding only a weak positive correlation to violations (r=.284, p<.05)[17]. This implies a stronger connection between the total assets held by an institution and the number of non-AML/OFAC violations during the sampled timeframe, and also supports the Dalton and Kesner's (1988) research from a monetary standpoint.

Findings: Research Question 4, Hypotheses 4, 5 and 6

The following series of analyses explore whether and what kind of relationships exist between AML/OFAC violations and inclusion into various Industry Success rankings and markers. Prior to beginning any analyses regarding the relationship between these industry rankings and AML/OFAC violations, a series of correlations were conducted to ensure that the Industry Success rankings were not overly related to each other in an effort to avoid any potential redundancies. As such, each series of Industry Success rankings (Best, Biggest, and Safest) were recoded into a new dummy variable that reflected the number of times a bank had appeared on each list within the sampled time frame (i.e. a bank that had appeared on 6 years' worth of the Safest Bank rankings was coded into the new dummy 'Safety Ranking' variable as a 6). These three new dummy variables were then analyzed through a Pearson correlation. The Pearson correlations for all three measures indicated a lack of any statistically significant relationship with each other as indicated in Table 5 below. Since these measures appear unrelated, three separate correlations between success ratings and violations were estimated.

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[17] Global Finance did not publish a Biggest 50 Banks for the year 2014 thus limiting the sample to 6 years rather than 7.

Table 5

Intercorrelations for Industry Success Rankings (N= 145)

	1	2	3
1. Times Appeared on Biggest Banks Rankings	-		
2. Times Appeared on Best Banks List	0.057	-	
3. Times Appeared on Safest Banks Ranking	-0.019	-0.08	-

Best Bank Analysis

The first of these correlations involved the relationship between the "Best Banks" listing as provided by Global Finance Magazine on an annual basis and violations. Unlike the other Industry Success lists that will be discussed in this research, Global Finance Best Banks typically included two types of winners: "Global Winners" and "Country Winners". For this research, however, only the *Global Winners* were included in the analysis as the sample of Country Winner-level data was limited[18]. Descriptive statistics indicated that there were between 8 to 17 "Global Winners" named each year within the sampled time-frame (2008-2014) for "World's Best Banks." These global winners were not presented in any particular order or comparative ranking with each other. A dummy variable was then created to provide a frequency count of how many times each bank was included as a *World's Best Bank* within the seven years sampled. As such, the final variable of use for this measure was a scale ranging from 0 to 7. Of the 145 included banks, 29 appeared at least once on GF's World's Best Banks list. Of those 29, 15 were included on the list only one time in the 7 year time frame, while one bank was noted as a *World's Best Bank* all seven years that were sampled (Further frequency distribution information is noted in Table 6 below).

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[18] It should be noted that in the 4 years that Country-level data was provided, annual Country Winners ranged from N=15 to 22 per year).

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The variable used to reflect the presence of AML/OFAC violations was also recoded to provide more variability for all analyses examining Industry Success markers' relation to AML/OFAC violations. This variable was created by partitioning out each category of violation (AML, OFAC, and non-OFAC/sanction-related) into yes (1) or no (0) responses regarding the presence of violations.

Table 6
Frequency of Times Appeared on "Best Banks" Listings

Times Labeled 'Best Bank'	Frequency	Percent
0	116.00	80.00
1	15.00	10.30
2	5.00	3.40
3	1.00	0.70
4	1.00	0.70
5	4.00	2.80
6	2.00	1.40
7	1.00	0.70
Total	145.00	100.00

However, rather than creating a dichotomous outcome as was used to assess Hypothesis One, these were summed, creating a variable with a range of 0 (no violations) to 3 (the bank possessed at least one of each type of violation). These data are described in Table 7.

Table 7
Frequency of AML/OFAC Related Sanctions

AML/OFAC/Sanctions Violations	Frequency	Percent
None	115.00	79.30
One of Three	16.00	11.00
Two of Three	10.00	6.90
Three of Three	2.00	1.40
Missing	2.00	1.40
Total	145.00	100.00

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A Pearson correlation was used to explore the potential relationship between the number of times a bank had been included on GF's Best Banks list and the presence of any AML/OFAC violations. Counter to the predicted directionality posed by hypothesis 4, this analysis reflected a weak, but statistically significant positive correlation between the presence of AML/OFAC violations and the frequency with which a bank appeared on the Best Banks list (r=.266, p<.01). Thus, the relationship expected in hypothesis 4 between being on the "Best Bank" list and likelihood of violations was rejected.

Biggest Bank Analysis

In order to assess the potential correlation between AML and/or OFAC violations and ranking as one of the Top 50 Biggest Banks, two additional series of correlations were conducted. The first examined the relationship between AML and/or OFAC violations (using the continuous version of the variable described in Table 7) and the number of times a bank was included as one of the top 50 Biggest Bank across 2008-2013[19]. Following prior research, it was hypothesized that the larger the bank, the more likely it was that a violation would occur. Consistent with that hypothesis, the relationship was positively correlated (r=.194, p<.05).

The second analysis examined the correlation between the numerical rankings for banks (1-50) for each of the sampled years (2008-2013) independently as provided by the GF survey and AML/OFAC violations coded as absent (0) and present (1). As depicted in the Table 8, few significant relationships were found between the presence of AML/OFAC violations and the

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[19] Please Note: 2014 data was unavailable for this specific Industry Success marker ('Biggest banks') so the time frame sampled is only 6 years in length as opposed to other Industry markers which reflected 7 years.

actual Biggest Bank rankings in each individual year[20]. The individual yearly association

between Biggest Bank and violations was significant in only two (2008, 2013) of the six cases

tested.

Table 8
Intercorrelations for "Biggest Banks" Rankings and AML/OFAC Violations

Biggest Bank Rankings	AML/OFAC Violations:			
	M	SD	r	p
Biggest Banks of 2008	8.60	14.77	0.179*	0.033
Biggest Banks of 2009	8.79	14.84	0.049	0.559
Biggest Banks of 2010	8.79	14.84	-0.009	0.916
Biggest Banks of 2011	8.79	14.84	0.125	0.137
Biggest Banks of 2012	8.79	14.84	0.101	0.229
Biggest Banks of 2013	8.79	14.84	0.216**	0.009

Note: N=143, *p< .05. **p <.01.

Safest Banks Analysis

In line with the other ranking analyses, examining the potential correlation between AML

and/or OFAC violations (using the continuous variable) and ranking as one of the Top 50 Safest

Banks was conducted through the use of two separate series of correlations. The first correlation

analysis indicated that the number of times a bank had appeared on the Safest Bank rankings

across the 7 year timeframe was positively correlated with the presence of AML/OFAC

violations, although the relationship was statistically insignificant (r = -.063, n.s.).

The second analysis correlated the numerical rankings (1-50) for each year independently

using the measure of Safest Banks provided by the GF survey to the presence of AML/OFAC

violations having occurred (1 = AML/OFAC violation was present, 0 = No violations). As

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[20] The Biggest Banks of 2008 have only 49 listed banks due to the merger of Groupe Caisse d'Epargne (ranked 28) and Groupe Banque Populaire (ranked 49) into Group BPCE. The ranking of 49 was used to represent the merged entity.

depicted in Table 9, only one significant relationship (2014) was found between the presence of AML/OFAC violations and the Safest Bank rankings.   Thus, the bulk of evidence related to hypothesis 6 rejects that hypothesis.

Table 9
Intercorrelations for "Safest Banks" Rankings and AML/OFAC Violations

Safest Bank Rankings	AML/OFAC Violations:			
	M	SD	r	p
Safest Banks of 2008	0.07	0.25	0.141	0.093
Safest Banks of 2009	8.41	14.71	0.037	0.659
Safest Banks of 2010	8.79	14.84	0.124	0.141
Safest Banks of 2011	9.53	15.08	0.052	0.539
Safest Banks of 2012	8.79	14.84	0.004	0.962
Safest Banks of 2013	8.79	14.84	-0.059	0.485
Safest Banks of 2014	8.79	14.84	-0.169*	0.043

Note: N=143, *p< .05.

While the findings noted above and the implications therein will be discussed in more detail within the next chapter, a brief review of results show support for a majority of the hypotheses stated within this research, as further depicted in Table 10 below. Overall, six of the eight hypotheses were not rejected. This suggests that numerous aspects of regulatory oversight and company dynamics predict banking AML/OFAC violation in manners commensurate with other forms of corporate crime, but that the presence of these AML/OFAC violations may have little bearing on a bank's perceived industry success.

Table 10
Summary of Findings

Hypothesis 1	Accepted
Hypothesis 2	Accepted
Hypothesis 3	Accepted
Hypothesis 3A	Accepted
Hypothesis 3B	Accepted
Hypothesis 4	Rejected
Hypothesis 5	Accepted
Hypothesis 6	Rejected

CHAPTER SEVEN:

DISCUSSION OF AML NON-COMPLIANCE AND BANKING INDUSTRY SUCCESS

The present study began by examining several aspects of regulatory oversight and company dynamics to explore whether variables like fine/settlement size, company size (both in personnel and assets), or frequency of non-AML/OFAC violations predict future AML/OFAC violations. Previous research had suggested that organizations with known patterns of wrongdoing may include a culture that supports and reinforces illegal activity and therein may be likely to experience further violations (Baucas & Near, 1991; Clinard & Yeager, 1980; Finny & Lesieur, 1982). As such, it was proposed that banks with AML or OFAC violations might possess "criminal cultures" that would lead to a greater presence of other forms of regulatory infractions. Analyses indicated that banks having more non-AML/OFAC regulatory infractions had a significantly higher likelihood of possessing an AML and/or OFAC related violation than those banks with little to no regulatory infraction history. This supports two related proposition. First, that AML violation may be a useful indicator of a more entrenched regulatory disregard/corporate malfeasance among banks, and that AML/OFAC violations can be used to predict engagement in non-banking violations by banking entities. Typically, one would suggest that future research is needed to replicate these results. In the present case, however, the assessment included all available AML/OFAC violation since 2008, and there is no remaining data source useful for replication at the international level. It might be possible to use national level data for this purpose to discover violations of national banking laws that are not also violations of international banking laws and to use those data for replication. Whether or not there are sufficient banking regulations of this type and sufficient number of cases is an unknown

and requires further research. Second, the observation that banks with AML/OFAC violations also have other types of violations has several additional implications. For example, the overlap between these outcomes may mean that similar cultural dynamics within banking institutions produce both banking and non-banking crimes by those organizations. Moreover, this finding suggests that some banks may be repeat offenders, recidivists or career offenders, and that future research should address this issue. Prior corporate crime research has explored these ideas in relation to some types of corporate offending (Lynch, Burns and Holcomb, 2005). Empirical studies of this issue are rare despite the fact that Sutherland (1949) made early reference to relevant empirical data on this subject. It also important to make note that the existence of "criminal cultures" is not the only potential cause of this observed relationship. Other explanations exist that cannot be tested due to the correlational nature of this research; for instance this relationship may be a product of how violations are being reported (self report vs. regulatory intervention/oversight), or differential levels of regulatory scrutiny in the industry based on history of previous violations or self report. It is possible that firms with a record of complete and accurate self-report in accordance with AML policy are less likely to receive additional scrutiny by regulatory bodies while firms whose infractions and/or lack of accurate reporting were discovered may well be subject to additional monitoring /enhanced scrutiny, thus potentially increasing the likelihood of further violations being found.

The present research also examined whether the punishment disparity noted in other forms of corporate crime control, whereby fines appear large in aggregate but are comparably small to firms' assets, was applicable to AML penalties. Three outcome of interest were found on this point. First, about 39% of banks were fined, and banks were more likely to experience non-monetary penalties in response to violations. This fact in itself suggests that fines are not

widely used and that fine amounts will be limited. Second, the range of fines employed was wide, ranging from $ 25,000 to $ 2 billion dollar in the most extreme case. A $ 2 billion dollar fine certainly appears significant in general, but in the specific case in which it was applied was quite small compared to the assets of the corporation penalized. Overall, the average penalty came to only 1.77% of a bank's assets. Finally, the $ 2 billion dollar fine against JP Morgan Chase accounted for 43% of all fines levied against banks during the time period under examination, significantly increasing the average fine per violation. For example, excluding the $ 2 billion dollar JP Morgan Chase fine, the mean fine against banks in the remaining cases drops by $ 112,000,000.

Third, no statistical significance was observed in assets held by banks before and after penalization, indicating fines have little to no impact on earnings and, thereby may have a limited deterrent effect against future violation. Although similar research is highly recommended comparing these fines to bank *profits* over time (rather than assets), as Barak (2012) alludes to with Wall Street more generally, this research seemingly provides further support of a regulatory climate in which AML fines also provide merely a 'slap on the wrist'.

It is possible that the results may have been affected by the nature of the sample. One issue is the survival rate of banks during the time period under examination. Within this sample of 54 banks identified as AML/BSA violators studied during the course of a seven year time frame, 25.9 percent (N=14) of banks have since failed, and another 13 percent (N=7) have subsequently merged into other entities and no longer exist as the entity found liable for AML/BSA violation. These data suggest that competition in the banking industry that leads to banks failures and mergers may increase pressures that can promote crime. Though this research cannot speak to causation and this information may be anecdotal with regard to the impact of

fines (as many of these banks were only subjected to Cease & Desist Orders), it may well imply a level of reputational or other damage that can not only deter future AML violation, but may well prove disastrous for the banks impacted thus evidencing some level of social control inherent in the current AML penalization process.

Following Dalton and Kesner's (1988) research on factors impacting the likelihood of corporate crime, another structural dynamic that was examined was whether the size of the bank impacted the likelihood of regulatory infractions occurring. Prior research has found that corporate size is a predictor of corporate violations, and that larger organizations are more likely than smaller firms to violate the law. This outcome has been found across a variety of areas of corporate crime research (Grant, Bergesen and Jones, 2002; Katou, 2013; Preechel and Morris, 2010. In the current study, firm size was measured by two variables, one which measured number of employees and the second which measured firm assets. Analyses showed, as expected, that larger numbers of both employees and assets are significantly correlated with increased regulatory infractions. This finding suggests that corporate size matters when it comes to banking violations, and that one way to control banking crime is to limit the size of banks.

The primary focus of this research was to evaluate the effectiveness of industry success rankings as a form of social control as it pertains to AML violations and to determine whether or not banks that ranked well on industry rankings were also less likely to have banking violations. A variety of rankings including safety, asset-based, and overall performance measures were used to assess their relationship to bank violations. The "Best Bank" rankings were based on a range of criteria including (but not limited to) profitability, management excellence, and competitive pricing. Based on the idea that reputational damage accompanies money laundering violation and that management excellence is exemplified through a record of avoiding fines, infractions, and

other serious violations of laws and banking regulations, it was expected that banks listed on this "Best" list have had relatively little to no involvement in such infractions. In contrast to that hypothesis, however, analyses showed a weak, but significant *positive* relationship between the presence of AML/OFAC violations and a bank's inclusion as one of GF's "Best Banks". This implies that as the likelihood of a bank ranking as one of the "Best Banks" increases, so too does the likelihood of that bank having an AML/OFAC violation. Thus, this result provides evidence that being ranked as a "Best Bank" has little to do with the likelihood that a bank has engaged in criminal behavior. This perhaps suggests that within the banking industry crime is considered to be such a routine form of behavior that it has no impact on "Best Bank" rankings or assumptions about what makes a bank a "Best Bank."

Similarly, results also indicated that more frequent inclusion on GF's "Biggest Banks" rankings was significantly related to an increased presence of AML/OFAC violation. Although analyses were less clear about the impact of the numerical rankings within this list, they indicate that increased assets correspond with an increase in the presence of AML/OFAC violations, which dovetails with hypothesis 3B's finding that total assets holds a significant positive relationship with non-AML/OFAC regulatory infractions. Taken collectively, these outcomes offer further support for Dalton and Kesner's (1981) reasoned importance of size dynamics in predicting the likelihood of involvement in regulatory infractions. However, they also imply that AML violations appear to have little to no impact on this form of industry success (i.e. sizeable assets, and or ranking as one of the Biggest Banks).

Based on principles of reputational damage, long term credit rating systems and risk profiles, and also the general ideal of "safety", it was expected that banks ranked as "safe" should be less prone to serious regulatory violations. This leads to the final hypothesis, that the

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rankings of banks listed on the "Safest" lists will be negatively correlated with the presence of AML and/or OFAC fines/citations/sanctions. However, this was not supported by the research. In reviewing the correlations, it was actually observed that only one of the seven annual measures of the correlation between "safest" bank and violations was statistically significant (Safest Banks in 2014). These data indicate that there is no distinguishable relationship between a banks' ranking as one of the industry's "Safest Banks" and the presence or lack of any AML/OFAC violations. Taken collectively, the analyses of the Best, Biggest, and Safest bank rankings are indicative of a pattern wherein AML violations appear to have very little impact on banking industry success ratings.

Overall, the analysis confirmed prior findings concerning corporate crime with respect to the effect of size on violations, and with respect to the observation that organizations with violations in different regulatory areas may have developed organizational cultures conducive to illegal behavior. Moreover, consistent with arguments from prior studies of corporate crime, fines were found to be relatively small in comparison to corporate assets, and only about one-third of the violators were penalized through the use of fines, perhaps the most serious punishment for banking crimes. The following section addresses the implications of these findings.

Implications

This study examined the social control of money laundering by banks, and questions about whether highly ranked banks and bigger banks committed fewer or more offenses than smaller and more poorly ranked banks. The primary form of social control evaluated was the rankings of the banks through safety, assets and overall performance. The analyses demonstrate a

pattern that these rankings are largely ineffective. Anti-money laundering violations appears to have little impact on or relationship to all three rankings of banking industry success. Although some of this may be due to other more predominant factors guiding the rankings rather than anti-money laundering concerns, this implication is that anti-money laundering is in no way controlled or even alluded to through these industry success rankings. Banks that violate AML/OFAC violations can receive different types of penalties or forms of social control. These are costly investigations that involve financial penalties, reputational damage, and the possibility that a penalized bank may subsequently fail. Whether those costs are justifiable – that is whether banking crime is deterred or sufficiently controlled and punished by existing forms of social control is questionable.   For example, with respect to all three of the industry's own success markers evaluated by this research, no relationship is found between those success rankings and banking violations. One might assume that banking industry success would have something to do with appropriate banking behavior as defined by banking regulations. This does not appear to be the case.

Another theme of note is the weight that a bank's assets appear to carry with respect to violations. Initial analyses revealed that AML/BSA fines are regularly a small fraction of what the bank's assets tend to be at the time of penalization/violation, and have little impact on future assets as well. Assets were also found to be significantly related to both non-AML regulatory infractions and AML/OFAC violations, in that as they increased, so did a bank's count or presence of these forms of penalties. Regardless of this fact, however, within the banking industry, sizeable assets are a beacon of safety, perceived to offer protection against liquidity and concentration risk, and able to cushion the fall from any risky investments or market conditions. With this, banks holding larger assets are easily marked as industry successes. However,

analyses show that these are the same firms that are more likely to have AML/OFAC violations and increased amounts of regulatory infractions. As such it can be argued that this standard for industry success is not only counterintuitive, but could potentially prove harmful to the financial industry. The banks receive positive industry attention for the abundance of assets they hold, which presumably lends itself to more assets, but then as those assets increase, so does the banks' likelihood of participation in AML/OFAC/regulatory violations increase.

As the data indicates, what banks appear to care most about is getting bigger and bigger, and not necessarily conforming with the law. This shows through in the forms of industry success markers that exist, and also the types of information that directly or indirectly drive those rankings. Moreover, their focus on size appears warranted when regulatory practices are examined. If a bank is big enough, and regulatory penalties continue to be neither proportional nor swift, then it is likely the bank can weather any storm caused by a banking infraction by having a competitive advantage – a large asset base -- rather than through sound practices as an avenue to continued success. However, what is not explained is why this occurs.

In line with Barak's (2012) arguments, the current research argues that this is likely a product of the political economy of capitalism rather than a derivative of any specific personality type or mind-set shared by those in control of our banking industry. In this political economy, decisions are largely made by the power elite, the group who control big corporations, sit atop major hierarchies, and through these ties are able to make highly consequential decisions (Mills, 1956). The decisions these power elite can make, however, are limited by the structural organization of society, which is in turn shaped by its economic organization. The elite's power comes from existing economic, social and political relations, thereby providing motivation for them to support the continuation of those power structures which advantage them. This

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research's focus highlights such an intersection of existing political and social structures that are producing bank crime through the manner by which banking regulations are applied and are then supported by the existing industry success rankings. To exemplify the power elite dynamic at work within the banking industry and as applicable to the present research, we need not look further than Stephen Green, also known as Baron Green of Hurstpierpoint. During the height of HSBC's money laundering violations, Green held the roles of Group Chief Executive (2003-2006) & Chairman (2006-1010) of HSBC Holdings plc. After stepping down from the role at HSBC he was then appointed to the British government to serve as the Minister of State for Trade and Investment, where he served a two year term[21]. Green's service record not only evidences some of the organizational intersection noted by Barak's (2012) research, but also implies a willingness of the both corporations and governments to overlook, or even encourage through continued service, a severe disregard for AML regulation.

The destabilization of our financial markets is feared to such an extent that when larger banks begin to fail, our government (historically) bails them out to preserve the safety and liquidity of the market, increasing their assets while simultaneously creating a "Too Big to Fail" mentality within the banking industry. Then, when sizeable AML or OFAC violations are uncovered, the current regulatory regime penalizes them with Cease & Desist Orders (which carry no financial penalty) or proportionally minuscule fines. Meanwhile, the industry rankings that *should* highlight success and promote social control of the banking industry, instead have been found to promote asset-gain alone, while offering the general public no discernible method to gauge the safety and soundness of their banks' practices. Banking crimes currently exist

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[21] https://www.gov.uk/government/people/lord-green-of-hurstpierpoint#biography (Accessed 6/6/2015)

largely underneath any public radar unless picked up by the free press, and are neither directly nor indirectly reflected by industry success markers thus allowing these trends to continue.

These observations point to the need for stronger regulation of banks, but also potential change to the method by which banks are regulated. First, the penalties must become more aligned with both the crime and also the means and profits of the institution. With fines averaging less than two percent of a firm's assets, it is highly unlikely that there is any deterrent impact present. As such, banking regulation reforms involving swifter investigations and more proportional penalty practices are also suggested. Additionally, corporate crime researchers have often suggested the need for criminal punishments and that offending individuals within the institutions need to also be punished to establish conditions that will lead to a reduction in banking crime (Cullen, Cavender, Maakestad & Benson, 2006). Criminal sanctions are rarely applied to AML violators at the entity/corporate level in lieu of Deferred Prosecution Agreements typically involving monetary settlements (as in the case of HSBC), and nearly never at an individual level. Future research should explore the potential impact and utility of employing criminal sanctions against not just the bank/corporation at fault, but also the individuals within that bank or corporation that contributed to or exacerbated the violation.

In addition to the existing regulatory framework that exists for banking crime, this research also examined its social control. As part of this, it is important to draw attention to the potential impact of reputational damage on banking crimes. Previous research supports the effect of reputational deterrents on corporate crime (Alexander,1999; Karpoff & Lott, 1993) Alexander's (1999) research found that reputational damage could result in corporate hardships including but not limited to terminated or suspended client relationships, increased employee turnover, and stock price decline. However, the true impact of reputational damage on banking

crimes, more specifically AML violation, may in fact be yet untested. At present, the public is likely to be largely unaware of such penalties. Very few cases are egregious enough to warrant the vast media coverage akin to what was seen in the case of HSBC or JP Morgan, and there are no industry rankings that identify which banks are truly 'safe', or that specifically reflect a bank's propensity for banking crimes. With the public so largely unaware, it becomes a question of how they would react if there was more awareness. Would reputational damage have a true impact on a firm's likelihood to violate AML regulations? And if so, how could this be used to supplement the regulatory ineffectiveness observed?

It is important to also examine the implications of this research with relation to the potential impacts of money laundering. As stated previously, anti-money laundering measures are affected to help preserve the safety and well-being of the economy, to prevent the funding of terrorism, and combat the growth of crimes and criminal organizations. When there is an ineffective system for the prevention of money laundering, the likelihood of these forms of crime and the risk to our financial system is greatly increased. For instance, HSBC's disregard for AML and OFAC policy allowed them to transact business for years with sanctioned countries including Sudan, Iran, Libya, and Burma; and to allow at least $881million in drug trafficking proceeds, including proceeds of Sinaloa Cartel in Mexico and the Norte del Valle Cartel in Colombia, to be laundered through HSBC Bank USA without detection (Case1:12-cr-00763-ILG). Even with the egregious nature and volume of their violations, the bank was not indicted on charges of money laundering. Rather, in December 2012, HSBC (i.e. all involved HSBC entities including HSBC Holdings plc, HSBC Bank USA, NA, and etc.) entered into a Deferred Prosecution Agreement in which it agreed to a series of compliance reform conditions and paid a

combined $1.9Billion for their violations. Meanwhile, their publicly available Fact Sheet[22] shows that (as of December 2014) HSBC Bank USA, National Association's assets alone total over $178 billion, with HSBC Holdings plc adding another $290 billion.

The case of HSBC shows how the current banking regulation system is not only ineffective at controlling money laundering, but more so, how this lack of effective control over money laundering has dire consequences to other criminal growth. HSBC helped to traffic nearly a billion dollars of drug money prior to finally being brought to justice, and then that justice was neither swift nor proportional to the crime. Even so, as of 2014, they ranked 27th among The World's 50 Safest Banks which leads the general public to believe they should invest their money with the firm, thereby increasing their profitability and therein the bank's ability to withstand future penalties should they recidivate.

Limitations

There are several data limitations to be considered with this research. The first is commonly referred to as the impact of the dark figure of crime, noting that statistical analyses cannot account for or predict the effect of crimes that have not been caught. Numerous corporate crime researchers have made note of the unknown potential impacts of this variable (Jamieson, 1994; Levi & Reuter, 2006; Reuter & Truman, 2004). Money laundering research also falls prey to this dark figure of crime, being unable to account for or explain instances of money laundering, AML program violations, and numerous other relevant violations that have eluded the regulatory and/or judicial system.

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[22]

https://www.us.hsbc.com/1/PA_1_083Q9FJ08A002FBP5S00000000/content/new_usshared/shared_fragments/pdf/hnah_factsheet.pdf

Another limitation specific to this research is the time-lag typically associated with both asset reporting and regulatory processes. Anti-money laundering violations are typically reported by regulatory bodies and enforcement agencies using dates that investigations were completed, fines handed down, or settlement agreements finalized, and are potentially focusing on events that occurred years ago. Meanwhile, companies report their assets with a time-lag ranging from months to an entire year based on when their fiscal year closes out, auditing requirements dictated, or annual reports are published. With so much variance embedded into the fining process and asset reporting, it proves difficult to directly assess the effectiveness of AML-oriented regulatory oversight in banking industry. Time lag holds similar potential limitations on the breadth of data that could be collected within the sampled seven year timeframe. Many investigations of AML and/or OFAC violations take years to conduct between the initial identification of a *potential* violation to the aftermath of a penalty being imposed. As this sample only included seven years of data (2008-2014), it likely could not have captured the full breadth of AML violations or regulatory infractions that may have been in process, or the full impact of those that were identified on the banks' Industry Success rankings.

The research was also limited due to the numerous hypotheses warranting examination through the use of Pearson correlations. Though this form of analysis shows how the variables related to each other, it could not allow the present research to speak to causation, which hampered some ability to show the true impact and predictive ability of anti-money laundering violations on the various industry success rankings. For instance, this research found that banks having more non-AML/OFAC regulatory infractions had a significantly higher likelihood of possessing an AML and/or OFAC related violation than those banks with little to no regulatory infraction history, and associated this relationship to the existence of criminal cultures. However,

there are other possible explanations, such as the potential for some banks to have been subjected to increased level of regulatory scrutiny over others based on their self-report of indiscretions or previous failures. Much of this research cannot account for the true causation, but rather evidences the existence of a series of relationships that require further attention from our field.

Directions for Future Research

This area of research is fairly new to criminology. As such, there is much potential for future study of both banking crime as it related to anti-money laundering, as well as financial industry success markers.

Based on the data available, the present study tested numerous hypotheses using correlations. Therefore it is plausible that the effects discovered here might be conditioned by other relationships that were not examined. Future research should include more multivariate tests where possible. Some suggested variables include: duration of existence [as a bank], services offered (e.g. savings vs. investment banking), global footprint (i.e. number of branches, number of countries), country of incorporation, profitability (year to year), individual criminal penalties, and civil litigation results.

This research examined the presence of a criminal culture within the banking industry. However, this culture was discussed at the organizational level, as this research specifically excluded any individual-level adverse news findings. Future research may elaborate on the dynamics of cultural presence of banking crime by not only including, but expanding upon individual-level findings. Due to the availability of data and our focus on the regulation of AML violation, civil litigation results were not included. However, these may also provide further

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clarity on banking crime as it is likely that banks, like many other corporate, settle civil claims outside of court to avoid further scrutiny.

Another dynamic that should be examined is the impact placed by a bank's country of incorporation. With the globalization of today's financial industry, we find that location strategy is of ever-increasing importance. With this, it becomes important to examine the potential impact of where a bank incorporates. We know that some countries are known for lax regulatory practices and taxation policy (e.g. Cayman Islands), and that this provides a competitive edge to those institutions that choose to incorporate there. With this globalization pattern and disparities that exist across locations, future research should ask whether the nation of incorporation affects violations. Research focusing on how banking crimes relate to patterns of globalization of the financial industry might also lend itself to the future comparison of banking crimes to other kinds of international crimes by corporations to get an idea of which types of industries commit more crime, (at least officially).

Due to the limited AML penalization data available, this research was unable to examine whether banks that recidivate are different that banks that did not recidivate. Future research should include this data ongoing in an effort to understand recidivating patterns among banking crime but more specifically anti-money laundering and OFAC violations.

Due to the post-hoc nature of this research and the availability of complete data, this research only sampled a seven year time frame. However, many AML investigations take years to complete between the identification of a potential violation, the course of investigation, trial and/or negotiation of penalty/settlement, public notification of affirmed violation, and finally the time lag that would follow with any potential fallout from said violation (i.e. reputational

damage, asset or rating impact, etc). This line of research would be well served by examining an elongated timeframe and larger sample. A more inclusive time sampling might better be able to identify patterns of asset flow, client base change, and reputational impact as well as gather more base-level data to use as controls to better isolate variables of impact. It would also be beneficial to attempt to coordinate with regulators at the beginning of an investigation in order to collect longitudinal data which might also assist in showing profile changes in banks from the point of first identification of an AML violation through the investigation period (during which it is likely many organizational behavior changes place due to physical regulator presence) and then after the violation has been assessed and publicized.

In the interest of replication as well as expansion and variety, further research should be conducted using other sources and varieties of industry success markers in an effort to expand upon the current research. Global Finance Magazine distributes these three rankings on an annual basis, and they are very specific in how they create these rankings, some with more subjectivity than others. Future research should search out other trusted banking sources with similar industry success ranking data for further exploration. Also, it is important to conduct similar research using industry success markers that are better able to partition out the impact of a bank's assets. These clearly have a sizeable effect, and are well embedded within the definition of success within the banking industry, but this has created difficulty in isolation/controlling such effects in order to look at other dynamics.

It would also be interesting to observe how changes over time in the general financial climate may predict AML violations, effectiveness of AML regulation, and patterns of reaction to differing climate. For instance, we know there was a financial housing market crisis around 2008 which impacted the banking industry greatly. We also know that a large portion of those

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banks cited for AML penalties between 2008 and 2014 became insolvent or merged with other entities to survive. What we cannot know based on the data available is to what extent the distressed climate of the financial market in and around 2008 may have played a role in those failings.

The population of AML/BSA violators should also be examined more closely in an effort to better understand why there is such a high proportion of those firms failing. It could be beneficial to know whether it was an effect of the banks' behaviors, the AML violation(s), the investigation or penalization process, or potentially the aftermath of that penalty. More generally, this also lends itself to future study of whether insolvency and mergers are impacted by regulatory infraction records.

Lastly, although it would require an unlikely level of cooperation from banks due to their notable and institutionalized concerns for the privacy of their practices and clientele, future research would also benefit from self-disclosure/survey research. Much of the limitation presented within current research is based on availability of the complete and accurate data and limited by the duration of time it takes to get finalized outcomes of AML and OFAC issues. If banks were willing to respond to anonymous survey research, this would alleviate issues of time-lag, and also produce more accurate industry data. For instance, if a bank were willing to disclose a violation in a survey *at the time of violation*, researchers would then be able to analyze how current assets, dynamics, and business practices impacted the actual occurrence of the violation rather than the regulatory penalization (which, again, can occur years later). Survey data would also help alleviate some of the dark figure of banking crime simply though the self-report of banking crime (whether provided anonymously or in an effort to mitigate the cost of an investigation).

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Conclusions

In conclusion, this research draws attention to the lack of studies of banking crimes and the importance of those crimes, highlighting how money laundering has importance for criminology as a field and with respect to the kinds of research criminologist should conduct. Criminology has historically been concerned with more mainstream crimes like drug trafficking and organized crime, but has yet to follow those crimes' funding and realize that effective crime prevention will include the prevention of money laundering. In order to have a holistic understanding of many crimes of interest to mainstream criminology, the research on how money laundering contributes to those crimes is a necessary evil and the effective prevention of money laundering should be of central concern. Once money laundering is of central concern, then the importance of researching banking crimes becomes evident as banks are the primary target for money launderers. Where there is ineffective regulation of banking crime, there is likely to be money laundering occurring, and where money laundering occurs other crimes are likely to flourish.

As is found in other forms of corporate crime, we also observed a theme of neglect toward the crimes of the powerful. In this research, this issue was highlighted in numerous areas. One example is the treatment of large banks with severe violations. The current system treats the larger banks, the corporation itself, as being among the power elite. Typically, because of their assets and standing within the banking industry, holding large banks fully accountable to their actions is seen as potentially disruptive or damaging to an already fragile financial industry. So instead of being held criminally accountable for their numerous and egregious criminal violations, they receive proportionally minute fines and sign agreements to do better in the future. Meanwhile, their senior executives, who likely share some level of culpability in said

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egregious violations, also escape any form of prosecution, criminal or otherwise, and are free to move into regulatory or governmental positions that help make high level decisions for the future of the financial industry.

The evaluation on the social control of banking crimes using existing industry success rankings also reflected an absence of effective social control in addition to a need for the banking industry to produce a wider variety and more targeted measures of industry success. The tested measures were found to be highly impacted by a select few variables (i.e. assets) and in and some cases might prove misleading to the general public.

Lastly, this research also calls attention to the ineffective state of AML regulation among banks, citing the need for AML/banking regulatory reforms. The current state of this regulation provides little more than a slap on the wrist for offenders even in the most egregious of AML violations. Regulatory practices should be reformed to include criminal prosecution of severe AML violations at both the corporate and individual level, as well as ensuring that fines are commensurate with both the crime committed by the bank and proportional to the firm's profits. Penalties should be assessed relative to profits so that penalties do not directly affect assets held by individual clients, who should not be penalized by the illegal behaviors of the banks in which their assets are held. At a minimum, this would help set a standard within the industry that AML violations will not be tolerated, but it may also help effect positive change at an organizational level by removing power elite responsible for promulgating a lack of concern toward AML violation that would keep the system ineffective as it exists and benefits them today.

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APPENDIX A:

ACRONYM GUIDE

AML: Anti-Money Laundering

AMLO: Anti-Money Laundering Officer

BBCI: Bank of Credit and Commerce International

BOL: Bankers Online.com

BSA: Bank Secrecy Act

C&D: Cease & Desist

CIP: Customer Identification Program

CTR: Currency Transaction Report

DPA: Deferred Prosecution Agreement

FATF: Financial Action Task Force

FBI: Federal Bureau of Investigations

FDIC: Federal Deposit Insurance Corporation

FI: Financial Institution

FINCEN: Financial Crimes Enforcement Network

GDP: Gross Domestic Product

GF: Global Finance Magazine

HIFCA: High Intensity Financial Crime Area

HSBC: The Hongkong and Shanghai Banking Corporation

IMF: International Monetary Fund

KYC: Know Your Customer

LE: Legal Entity

OCC: Office of the Comptroller of the Currency

OFAC: Office of Foreign Assets Control

SAR: Suspicious Activity Report

SUA: Specified Unlawful Activities

UID: Unique Identifier

US: United States

USA: United States of America

USA PATRIOT: Uniting and Strengthening America by Providing Appropriate Tools Required
to Intercept and Obstruct Terrorism

APPENDIX B:

WORLD CHECK DATA COLLECTION & CLEANING PROCESS

World Check searches were conducted by copying and pasting the names provided within

the Top 50 lists into the World Check system. Once pasted into the name field, the type of search

was updated to a "part" search (as opposed to the "exact" match default setting). This parameter

ensures the search will be conducted using a fuzzy logic matching system, which captures

matches despite slight name variations, spelling errors, nicknames, and language/character

variations. This setting was used in order to ensure that true match hits were included in results.

However it also regularly produced results beyond the true matches.

In cases where 100 or more profiles resulted from a part match search of the entity name

provided, the search was captured for record-keeping purposes, and then re-run using the

"Exact" match parameter. The results of this search were also captured. In the event that the

"exact" match search also resulted in 100 or more profiles, a third search was conducted. This

search reverted back to the "part match" setting, but would include the country specified for the

bank within the Top 50 results. In the event multiple countries were identified, this would be

done multiple times (as needed). In the rare event that a part match screening specifying country

still resulted in 100 or more profiles, the results screen would be captured for record keeping, and

a fourth search would be conducted using the "exact" match parameter and the specified country.

As an example of this process, please note that the search for "ING" (part match) resulted in more than 50,000 potential profile matches. The second screening of ING (exact match) resulted in 288 potential profile matches. The third screening on ING (part match / country: Netherlands) resulted in 473 potential profile matches while ING (part match / country: Belgium) resulted in 269 potential profile matches. Finally, the fourth round of screenings on ING (exact match / country: Netherlands) resulted in 21 potential profile matches, while the (exact match / country: Belgium) resulted in 6 potential profile matches. These 27 profile records were pulled and housed as individual records.

False Positives

Once a search was conducted and all potential profile matches saved[23], the process of identifying any "false positives" began. Due to the part matching system, many of the searches contained results that would be designated as a "*false positive*"; essentially, a profile listing adverse news of an entity that had a similarity in name, acronym, affiliation, or etcetera, but that was NOT a true match to the bank being searched.

Following industry standards, in order to designate a profile as a false positive, a profile had to contain at least two discrepancies that would differentiate it from the bank being searched. Such discrepancies might include differences in name, entity type (corporate/ bank versus organization[24]), business type (i.e. a bank versus a broker/dealer or insurance company), and

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[23] Please note – Profiles indicated as having Category Types including: '*Individual*', '*Political Individual*' and '*Diplomat*' as well as any profiles specifying a human/individual's naming convention were not pulled because the focus of this research is on corporate entities (banks) and such reports would include sensitive (potentially adverse) information on individual persons rather than corporate entities. Examples of Category Types subject to inclusion for this research included (but were not limited to): 'Corporate, Bank', or 'Organization' and potentially 'Terrorism'.

[24] Within the World Check system, an "Organization" typically refers to a regulator, governmental body, or other oversight/authority issuer. Although these were pulled due to their status as a legal entity, there were no cases in which one was deemed a true match to the target of a search.

etcetera. If two distinct discrepancy criteria could not be found, *or* if there were doubts that the profile was a false positive in spite of finding two distinct discrepancy criteria[25], further research was performed via the internet to provide clarification. Any such research was saved to the relevant profile's folder for record retention purposes.

Bank Branches

Bank branches are not typically considered to be a distinct legal entity. For instance Philippine law recognizes that bank branches are not separate entities apart from the home office and that a branch obligation is an obligation of the bank as a whole. The United States has multiple outlooks on the legal distinction of bank branches as is briefly described below:

> "Although a branch of a bank is not a separate juridical entity from the bank of which it is a component, U.S. law treats branches as separate from the head office and other branches of a bank when such differentiation is appropriate for various purposes. Branches are a hybrid structure, at the same time both an integral part of the banks of which they are merely offices and separate legal entities for a number of U.S. regulatory and commercial law purposes. This feature of bank branches is a central tenet of federal banking statutes, and the law governing U.S. branches of foreign banks in particular.
>
> At times the status of a U.S. branch of a foreign bank under a particular statutory scheme is explicit. Such is the case with the U.S. legal treatment of U.S. branches of foreign banks in insolvency. As discussed below, U.S. law treats those branches virtually as separate entities in insolvency.
>
> In other circumstances, a particular statute does not explicitly address the status of U.S. branches of foreign banks, and the treatment has to be arrived at through an analysis of the purpose of the statutory scheme."
> (http://www.davispolk.com/files/uploads/Dodd-Frank%20documents//Dodd-Frank.white.paper.U.S.Branches.Foreign.Banksapr12.pdf)

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[25] Such as in the case of a name change or merger/acquisition.

With this logic in mind, paired with the understanding that OFAC and AML violations will typically impact the U.S. branch of a foreign bank, any adverse news results of a U.S. branch were included into the main bank's adverse news results, inclusive of regulatory fines, and AML and OFAC violations. However, other *non-U.S.* branches were deemed as False Positives for the purpose of this research as it would take a breadth of understanding and interpretation of foreign law and regulation that is beyond the scope of the present research to have included all foreign branches' adverse news. In summary, where the main branch of a bank was identified within the Industry Success rankings, and the adverse news research provided numerous branches with adverse news, only US branches' adverse news would be included for the purposes of this research, and this would be in addition to the main branch's adverse news results.