



Understanding AML

Its Origin and Evolution

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The term money laundering is presumed to have originated when Al Capone, America's most famous organized crime leader (operated from 1925-1931), invested illegitimate money obtained through sale of drugs and alcohol, and prostitution during the prohibition period into cash-driven laundromat businesses. These laundries were used as covers for the dirty money as this money was mixed with the money used to purchase assets, pay employees, and cover the business operation expenses, thereby making all the money appear legitimate and clean. Al Capone's methods of creating complex financial networks and using offshore accounts and shell companies are still used by modern-day financial criminals to obscure money trails of illegal money.

Money laundering activities comprises:

1. Placement: Money obtained from illegal sources is placed into a legitimate business.
2. Layering: The money is then put through a series of transactions to disguise or obscure its origin. Legitimate assets are purchased to legalize the money and it is transferred.
3. Integration: The money that's obtained from these transactions that has been cleaned from being used in a legitimate manner is then integrated into legitimate business as clean money.

Anti-Money Laundering (AML) is the set of policies, procedures, and technologies that prevents money laundering. It is implemented within government systems and large financial institutions to monitor potentially fraudulent activity.

The Evolution of Anti-Money Laundering

AML regulations began taking effect from the passing of the Bank Secrecy Act (BSA) in the US in 1970. The BSA is the foundational law for AML and was passed in response to the growing trend of criminals using secret foreign bank accounts to launder money. The law requires financial institutions to maintain records and report certain transactions to help detect and prevent money laundering, terrorist financing, and other financial crimes. Administered by the Financial Crimes Enforcement Network (FinCEN), the BSA mandates filing Currency Transaction Reports (CTRs) for cash transactions over \$10,000 and requires the reporting of suspicious activities, providing a crucial tool for law enforcement to combat illicit financial activities and ensure financial transparency.

Other jurisdictions across the world, including the European Union, also adopted similar AML measures as the US. In 1989 a group of countries (G7 - Canada, France, Germany,

Italy, Japan, the United Kingdom, and the United States) and non-governmental organizations (NGOs) formed the Financial Action Task Force (FATF), an inter-governmental body promoting international standards against money laundering. The role of the FATF was to examine money laundering techniques and trends, review the action already taken at a national or international level, and to set out measures needed to combat money laundering. In April 1990, the FATF issued a report containing a set of *Forty Recommendations* which aimed to provide a comprehensive plan of action to fight money laundering.

Following the 9/11 attacks, the scope of Anti-Money Laundering (AML) was expanded to include Countering the Financing of Terrorism (CFT) and the Financing of Weapons of Mass Destruction (WMD). The USA PATRIOT Act, passed in response to the attacks, spearheaded this change by instituting stringent new rules. This expansion redefined the global financial security landscape.

The USA PATRIOT Act

Signed into law on October 26, 2001, the Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism (USA PATRIOT) Act made significant changes to AML regulations. Title III, known as the "International Money Laundering Abatement and Financial Anti-Terrorism Act of 2001," was particularly influential.

The provisions in the law impacting financial institutions included:

- **Mandatory AML programs:** Requiring financial institutions to establish written programs with internal controls, a compliance officer, training, and an independent audit function.

- Customer Identification Program (CIP): Mandating that banks and other financial institutions verify the identity of new customers to ensure they are not on government watchlists.
- Enhanced Due Diligence (EDD): Requiring financial institutions to apply higher scrutiny to high-risk accounts, including correspondent accounts from foreign banks and private banking for foreign persons.
- Expanded reporting: Expanding the criteria for filing Suspicious Activity Reports (SARs) to include potential terrorist financing.
- Restricted shell banks: Prohibiting US financial institutions from doing business with foreign shell banks that do not have a physical presence in any country.
- Information sharing: Creating new provisions for cooperation and information sharing between financial institutions and government agencies.

The international community, led by FATF, also took immediate action. The FATF expanded its 40 Recommendations on money laundering to explicitly address terrorist financing and, later, the financing of Weapons of Mass Destruction (WMD) proliferation.

The framework introduced by the USA PATRIOT Act and FATF recommendations laid the groundwork for subsequent reforms, including the Anti-Money Laundering Act of 2020, which further modernized and strengthened AML efforts.

Other important international organizations in the fight against money laundering include the International Monetary Fund (IMF) and the United Nations (U.N.), and programs include the Council of the European Union's Anti-Money Laundering Directive (AMLD) and the Basel Committee on Banking Supervision's Customer Due Diligence (CDD) for Banks.



Quantum Data Engines is a reg-tech company that helps financial institutions detect, manage, and report financial crime more effectively and efficiently.