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## Banks' Level Factors Affecting the Effective Implementation of Anti-Money Laundering Practices in Nepalese Banks: An Employee and Customer Perspectives

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## Banks' Level Factors Affecting the Effective Implementation of Anti-Money Laundering Practices in Nepalese Banks: An Employee and Customer Perspectives

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### ABSTRACT

**Purpose:** Money laundering can affect global macroeconomic projections, currency markets, and financial stability by fueling shadow economies. Thus, the efficiency of the Anti-Money Laundering (AML) procedure must be investigated. Understanding such elements may help prevent money laundering. This necessitates studies to raise awareness and emphasize its importance. This study sought to assess customer understanding and examine the factors that affect the efficient application of AML regulations in Nepalese banks.

**Design/Methodology/Approach:** This study includes responses from 201 bank consumers and 156 bank employees. The study focused on customers' AML awareness and how bank employees implement AML regulations in their respective banks.

**Findings:** According to the study, consumers apprehend money laundering, terrorist financing, and their implications. According to bank employees, customers are unaware of money laundering and its consequences. Banking and financial institutions should prioritize education and awareness to improve the implementation of anti-money laundering regulations. Control over company sophistication, business ethics, customer awareness, and the AML system all have a favorable influence on Nepali banks' AML policies. The analysis reveals that business sophistication control is quite important.

**Originality:** The study focused on consumer and employee AML knowledge, revealing ground-level perspectives. The study found the variables related to the bank's management and compliance department's views on AML policy implementation. This research assists government agencies and policymakers in developing national anti-money laundering measures and aids academics in AML procedure implementation.

### KEYWORDS

Anti-Money laundering,  
AML, Nepalese Banks,  
Nepal.

### JEL

### CLASSIFICATION

K10, G20, G28

## I. Introduction

Anti-Money Laundering (AML) practices are critical to the functioning of the global financial system. Banks play a central role in ensuring compliance with AML regulations, and they face significant risks if they fail. Several bank-level factors can influence AML practices, including organizational culture, leadership, technology, and governance structures. UN Report (2021) estimates that 2.7% of global GDP gets laundered annually. Bribery costs between \$1.5 and \$2 trillion annually worldwide. Underdeveloped countries are particularly harmed by clandestine transactions. Most illegal money is

laundered through businesses that offer financial services, such as banks, finance companies, insurance companies, and capital markets (Ejanthkar & Mohanty 2011). Money laundering is the process of turning money that came from illegal activity or illegal sources into a legal way to pay for something. "Terrorism financing" (TF) occurs when these assets or finances fund terrorist actions. TF requires a good understanding of Money Laundering (ML) (Mukhtar, 2018). The Financial Action Task Force tracks money laundering and terrorism funding worldwide (FATF). FATF Standards combat global organized crime, corruption,

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and terrorism. This helps to track the money that is used to pay for illegal activities like terrorism, human trafficking, and the sale of illegal drugs.

An inadequate interrogation system, a poorly trained bureaucracy, a lack of long-term strategy and standards, and a huge informal transaction with India made Nepal an ideal place to launder money, according to Asia Pacific Group (2011). FATF's February 2010 report on Nepal's ML/FT situation highlighted a strategic AML shortfall. Nepal was removed from FATF's list of AML-deficient nations on June 27, 2014 (Knowyourcountry.com, 2021).

Nepal's enhancements to its anti-money laundering and counter-terrorist financing systems, as well as its legal and regulatory framework to fulfill strategic gap obligations. Asia Pacific Group (2011), Mutual Evaluation Report on Nepal's compliance with anti-money laundering and counter-terrorist financing rules determined that Nepal was Compliant for 1 and Largely Compliant for 3 of the FATF 40 + 9 Recommendations. Partially Compliant or Non-Compliant for all six Core Recommendations.

Organizations must understand money laundering to combat it. Money laundering involves placement, layering, and integration. Placement puts unlawful or illegal money in respectable financial systems like banks. Layering hides money's source through transactions and bookkeeping. Final integration involves withdrawing the now-legal money from the real account. Laundering and terrorism financing have non-financial effects. They exacerbate societal woes by affecting the economy. They destroy the economy and are a social evil (Mukhtar, 2018). Viritha, Mariappan, and Haq (2015) claimed that because illicit money affects a country's economic and security, many governments know how important it is to identify and confiscate illicit funds for their citizens' safety.

According to FIU-Nepal (2020), banks and financial institutions must record foreign currency transactions of more than Rs. 0.5 million in a single day, plus cash deposits or withdrawals of more than Rs. 1 million. In fiscal year 2019/20, out of total Threshold Transaction Reporting (TTR) 24,85,361, 90.78% was reported by banks and financial institutions, followed by insurance firms and cooperatives. Suspicious Transaction Reporting cases totaled to 333 cases from total TTRs. Over half (185) of 2019/20 instances were tax evasion related. Most company tax avoidance involved personal savings accounts. Similarly, 21.32 percent of the incidents were tied to high-volume transactions conducted through a personal account.

Growing Nepal is under peril. Medium anti-money laundering measures and medium-high banking industry vulnerabilities. AML enforcement is minimal compared to its scope, goods, asset volume, and transactions, and business-related risks make the supervisory process and practice ineffective (FIU-Nepal, 2020). Similarly, International Corruption Index ranks Nepal 33rd and World Governance Indicator – Corruption Control ranks Nepal 27th (Know your Country, 2021).

To make white money, tainted money must be recycled. Because bank customers must help combat illegal activities. Despite its large scope, limited research has been conducted in Nepal in regards of Anti-money laundering implementation, notably Thapa (2015), Joshi and Shah (2020), and Biswakarma and Koirala (2021). OECD (2019) stated money laundering is changing. Cash-based companies typically launder money. Laundering money involves cryptocurrency, funnel accounts, offshore bank accounts, and cooperatives. Awareness is needed finding unlawful money. It prevents money laundering.

Various studies' like Buchanan, (2004), Reuter and Truman (2005), Gelemerova, (2011), and Vitvitskiy et al. (2021) work

has shed light on global and national anti-money laundering systems, as well as BFIs' AML/CFT compliance. Several international studies like Carrington and Shams (2006), Verdugo (2008), Verdugo (2011), Reddington (2011), Beekarry (2011) and Sultan and Mohamed (2022) have examined AML regimes, their effectiveness, consumer knowledge, AML laws, the relationship between AML and CFT, factors affecting money laundering, anti-money laundering regulation and banking sector stability, and Nepalese bank adoption of AML requirements. Nepal's money laundering has garnered notice recently. Technology and business complexity have enhanced banking services. The FY 2022/23 budget prioritizes financial services for most transactions, including the National Payment Switch, payment cards, retail payments, QR code payments, digital payments, and wire transfers. Despite regulations, use and trade of cryptocurrency has increased significantly over the previous decade in Nepal (Bhandari, 2022). These improvements raise the question of whether banking business knowledge controls or aids money laundering. The central bank, financial institutions, and government are developing AML regimes to combat ML. AML law efficacy and implementation issues are studied internationally. Few Nepalese studies exist.

This study contributes to a better knowledge of AML implementation and the elements that influence its efficacy. Nepal carried undertaken multiple AML investigations. This study investigates how Nepalese banks apply AML as well as analyzes client AML knowledge, providing a chance to investigate AML implementation and security awareness. The identification of factors affecting the efficacy of AML practice implementation can provide insight into the bank's management, and more specifically the compliance department's perspective on the items that are crucial for effectively adopting AML standards. This study

focuses to explore Nepalese Banks' customers' awareness of AML standards while measuring factors affecting effective implementation. The paper focused to the following questions between these concepts:

- What factors affect the effective implementation of AML practices in Nepalese banks?
- What level of awareness do the bank customers have on Anti-money laundering (AML) practices from Bank employees' perspective?
- What level of awareness do the bank customers have on Anti-money laundering (AML) practices?

The rest of the paper is organized as follows. Section 2 presents the literature review and hypotheses development. Section 3 explains the data and methodology. In Section 4 the findings and discussion are presented and Section 5 concludes.

## II. Literature Review and Hypotheses Development

### *Theories underpinning money laundering*

*Economic Theory:* Adam Smith's classical economics lists two influences on behavior. On one side, everyone rationally maximizes their utility. This governs illegal wealth accumulation. Supply and demand determine a firm's usefulness via projected expenses and returns. In the usual Smithian world, the government protects its citizens from injustice and violent crimes because people and things are sometimes guided by an unseen hand toward purposes they did not intend. Smith supported natural liberty. As long as they don't break the law, people can follow their own interests and compete using their own resources in such a society. Illegally getting money affects citizens. Classical economics makes dubious assumptions. State policies encourage rivalry between institutions. This could slow society's development toward riches and dignity (Geiger and Wuensch, 2007).

*Crying Wolf Theory:* Overreporting or "crying wolf" devalues reports. Formal ML analysis began with overreporting. Banks report abnormal transactions. Banks are fined for not reporting ML, and agencies can't use the data. Avoiding penalties, banks report fewer suspicious transactions, distorting data. Financial constraints comprise the formal approach. Banks and governments miscommunicate. Accuracy—not verification—is the objective. Secondly, the bank lacks reporting incentives. Thirdly, Banks are punished for not declaring ML transactions, not hiding evidence. Since banks don't know what's happening, every transaction is ML. Fourthly, Banks must report suspicious transactions. Fifth obstacle is the unverifiable bank transaction signals. "Wolf-crying" is harmful. Since banks cannot communicate signals with the government, reporting is important (Takáts, 2007).

### *Empirical Review*

Chaikin (2009) investigated Switzerland's suspicious transaction reporting system for anti-money laundering. Banks report suspicious transactions to Intelligence Units-Finance under worldwide AML systems. Suspicious Transaction Reporting (STR) systems follow national and Financial Action Task Force (FATF) AML guidelines. FATF meetings and original sources analyze STR systems. The investigation found FATF assessments of a country's conformity with international standards unbiased, expert-driven, and consistent. Unreported suspicious transactions threaten the Swiss STR system. Swiss STR is efficient because mandated reporting freezes huge sums of money.

Jun and Ai (2009) study customer due diligence (CDD) in China utilizing data from industrialized countries and international organizations. They draw this conclusion from global CDD laws and China's CDD compliance approach. China

has implemented FATF-mandated CDD since 2007. Since 2007, Chinese banks have regularly upgraded CDD and KYC. Compliance strengthens AML controls. China's laws promote practicality and technological innovation while meeting international norms. ML/FT operations hurt economic growth, exchange rates, and the legal system's ability to fight corruption and the informal sector (Department of Money Laundering Investigation, Nepal, 2021).

Young (2014) explored Jamaican money laundering and UK-Jamaica financial criminal links. Insufficient legislation leaves Jamaica vulnerable to money laundering via remittances. UK drug traffickers may send money home to Jamaican offenders. India's Financial Intelligence Unit (FIU) assessed suspicious transaction reports (STRs) for anti-money laundering (Viritha, Mariappan & Haq 2015). Researchers examined FATF proposals on money laundering conviction and seizure. From 2006-2007 to 2011-2012, a descriptive study using FIU-India and FATF data. STRs increased significantly during the research. Prosecutions and confiscations do not measure money laundering prevention. AML/CFT issues and their security implications are unknown to Ghana (2016). The research suggests that the financial information unit and the NGOs Standards Commission collaborate on anti-money laundering, anti-terrorist financing, and donation acceptance regulations. The financial information division will work with religious groups and the Ghana Education Service's Islamic Education Unit to promote ML/TF projects. Ghana needs financial crime lawyers.

Qureshi (2017) cited Bank of New York accounts laundering \$7.1 billion in the late 1990s. The bank was acquitted and its employees blamed. In 2005, the bank admitted to violating AML requirements and paid a \$38 million punishment. Standard Chartered Bank laundered billions in Iran in the 2000s. The bank helped Iran

complete 60,000 \$250 billion transactions. The bank paid \$340 million for facilitating illegal transactions and money laundering. Money laundering and terrorist financing threaten world peace, security, law and order, the financial system, economic prosperity, and civilization. Crime promotes unlawful financial transactions, WMD development for terrorism, tax system undermining, and openness decline. AML/CFT prevents financial institutions from laundering assets. These policies need CDD/KYC (Financial Information Unit, 2020).

### *Hypotheses development: Dimensions of effectiveness of AML practices*

#### *Employee Training and Development*

AML programs, according to Shanmugam and Thanasegaran (2008), ensure personnel competency. AML awareness, forensic accounting, investigation competency, and mutual legal for asset confiscation and criminal cases are all part of AML. AML training, according to Chisenga and Phiri (2011), boosts efficacy. According to Viritha (2016), AML training is insufficient, which means that while employees are given AML training, it is insufficient to meet their need to carry out AML activities. As a result, it is critical to give adequate and high-quality training to bank workers. According to Biswakarma and Koirala (2021), employee training has a minimal impact on AML practices in Nepalese banks. The AML awareness of Nepalese bank workers was investigated. According to the report, the risk of AML is larger since banks do financial intermediation. According to the findings, banks workers comprehend ML and AML. Employees are less knowledgeable with FIU's NRB department. The study recommends banking institutions to provide ongoing training and development to AML-involved front-line and back-office employees. According to Government of Nepal (2020), predicate offense investigators require AML/CFT

training as well as a standard financial crime investigation manual. Furthermore, Bahrin, Yusuf, Muhammad, and Ghani (2022) discovered that employee competence influences the effectiveness of AML systems. A frontline banker training and development program focuses on recognizing risks in suspicious transaction reports (STRs) and applying customer due diligence (CDD) standards. The hypothesis based on the review formulated as:

*H1: Employees trainings and development regarding AML has an effect on effective implementation of AML practice in Nepalese banks.*

#### *Control Over Business Sophistication:*

According to Gill and Taylor (2004), the implementation of AML legislation in the UK financial industry generated concerns about its effectiveness. Despite the FSA's encouragement for enterprises to adopt a risk-based strategy, many respondents felt the limits would have alienated their long-standing clients if they had been in place when these accounts were opened. Many people despised the regulations' rigidity. According to some, KYC standards are disproportionate to the risk of money laundering. According to Leong (2007), despite government, law enforcement, professional, and private financial efforts, money laundering and terrorism funding remain threats. Tighter regulation may burden the banking industry even more. According to Lucian (2010), the globalization and regionalization of international organizations resulted in open borders. The use of sophisticated technologies and open borders by criminal groups is highlighted. Money laundering becomes more difficult to track as business complexity increases. National regulations are required for anti-money laundering. Money laundering should be reduced as a result of new legislation. Unger and Hertog (2012) discovered that estimating unlawful revenues and laundering trends over time was problematic. Criminals go from less-

regulated financial markets to the more-regulated banking industry, as well as between these two industries and other businesses. Electronic payments and trading are utilized to destroy black money. Biswakarma and Koirala (2021) discovered that company control had a moderate effect on AML practices. The hypothesis based on the review formulated as:

*H2: Control over business sophistication has an effect on effective implementation of AML practice in Nepalese banks.*

### ***Business Ethical behavior***

Vaithilingam and Nair (2007) investigated the application of AML in 88 developed and developing countries. According to the report, strong courts and ethical banks minimize money laundering. According to Parashar (2010), ethical behavior by banks minimizes illegal money flows. Money laundering should be discouraged by increasing public awareness of its severe economic consequences. The Nepal Bankers Association (2020) defines ethical bank behavior as fairness, service standards, customer privacy, responsibility, and transparency in delivering information and judgments. Any suspicious NBA transactions are also documented. Because of unethical banking practices, money laundering and other financial crimes are on the rise. Khan (2021) conducted a qualitative deductive investigation. Professional practices that are ethically compliant were also demonstrated to avoid money laundering. Some of these responsibilities include establishing severe codes of conduct for financial transactions, informing workers about the consequences of illicit AML activities, and implementing effective management and control mechanisms to monitor institutional wrongdoing. Biswakarma and Koirala (2021) investigated the AML activities of 136 Nepalese bank employees. Among the six characteristics examined, respondents agreed most with 'bank ethical behavior,' meaning that it has the most influence on

AML implementation. The hypothesis based on the review formulated as:

*H3: Business ethical behavior has an effect on effective implementation of AML practice in Nepalese banks.*

### ***Customer awareness***

FIU-Republic of Mauritius (2006) examined adult ML knowledge and risk perception. All stakeholders know about anti-money laundering laws and the FIU's role in fighting money laundering. Respondents favoured teaching clients about money laundering and anti-money laundering to prevent money laundering and terrorism financing. Singh (2009) remarked at an Indian money laundering conference that a lack of client knowledge hinders AML. Poor, illiterate Indians fear banks. Hawala allows financial transfers without documentation, sending money through banks. Hawala offers bank-like remittances with less paperwork, reduced rates, security, and secrecy. It's prevalent because people don't realize it's illegal. Gerstein and Hervieux-Payette (2013) advise educating clients about money laundering and terrorism financing. Viritha and Mariappan (2016) examined client AML acceptability in Indian banks. Banks as ML/TF conduits, reporting, AML/CFT legislation, and FIU roles are poorly understood, according to the poll. Indian customers knew about ML and ID. Participants viewed AML measures neutrally. Latif and Abdul-Rahman (2018) found that a lack of client awareness prevented AML adoption in six Malaysian Islamic and mainstream banks. Customers are oblivious of money laundering and financial wrongdoing, the report states. Customers are ignorant that banks launder money and fund terrorists. KYC and identity requirements are unknown to customers. The study suggests banks and local media work together to raise financial literacy and knowledge of money laundering and terrorism financing. Public and business sectors lack AML/CFT

understanding, according to Nepal Rastra Bank (2020). Regulators prioritize KYC over AML/CFT. Random, unresearched regulatory reporting. Joshi and Shah (2020) examined Nepalese consumer AML awareness and AML regime acceptability. The study linked AML awareness with acceptance. Nepalese bank clients knew some about ML, TF, AML, KYC, AML regulation, and AML investigating authorities, the study found. The hypothesis based on the review formulated as:

*H4: Customer awareness has an effect on effective implementation of AML practice in Nepalese banks.*

#### **AML system**

A strong AML-CFT framework must include enforcement measures that enable international collaboration (UNODC, 2009). Russian financial regulator Subbotina (2009) evaluates banks' AML compliance. Examining the regulator's financial institution regulations, practitioner interviews, and banking activity yielded a comparative analysis. The survey found that banks and financial organizations violate AML laws. This raises questions regarding banks' regulatory compliance. Ahmed (2017) suggests addressing Bangladesh's social and economic issues before applying the AML framework. IFC (2019) recommends AML regulations, procedures, and internal controls to reduce risk assessment risks. They must prevent, detect, and report suspicious activity, meet local norms, and establish strong internal control and risk management. Banks need risk-based policies, processes, and controls. Higher-risk clients, things, and situations may require more restrictions and monitoring. Ofoeda, Agbloyor, Abor, and Osei (2020) say AML law helps developing countries' banking industries. Asia-Pacific-focused FATF associate member APG APG communicates using FATF guidelines to prevent money laundering and terrorism funding. Nepal joined APG to implement

global AML/CFT standards. Nepal is affiliated with FATF through APG. The Money (Asset) Laundering Prevention Act, 2008, and its second amendment govern Nepal's AML/CFT laws (Biswakarma and Koirala, 2021). Nepal's Administrative Financial Information Unit (FIU) was established on April 21, 2008, to collect, process, analyze, and disseminate financial information and intelligence on suspected money laundering and terrorism financing activities to the money laundering investigation department, other law enforcement agencies, and foreign FIUs (Financial Information Unit, 2021). Issah et al. (2022) examined the effects of AML efficacy on Africa's banking industry. A study found that anti-money measures improve banking. The hypothesis based on the review formulated as:

*H5: AML system has an effect on effective implementation of AML practice in Nepalese banks.*

#### **Money laundering's effects**

Laundering is how the mafia transfers illegal funds into front companies. Money laundering is transferring criminal money via a complex banking system. Money laundering is the process of concealing or transferring illegally obtained monies or assets. This variable measures bank customers' awareness of ML, its economic impact, and its link to terrorism financing. Money laundering and terrorism funding are intricately linked, thus it's important to understand both (Mukhtar, 2018). Raising money to fund terrorism. Government of Nepal (2008) defines terrorist financing as any money for an act that intimidates a people or coerce a government or international organization to murder or seriously hurt a civilian or anyone not actively engaged in hostilities in an armed conflict. ML and TF go through banks. Bank customers are assumed to know TF.

*Bank for ML/TF:* Unknowingly, banks and other financial institutions may transmit or deposit unlawful funds. Criminals and their



collaborators use the financial system to send money between accounts, conceal the source and owner, and deposit cash in bank vaults (Basel Committee on Banking Supervision, 1988).

Identification standards and importance: Know Your Customer (KYC) is one of the tools of Anti-Money Laundering. Due to its close interlink, it's used as a single variable. Anti-money laundering measures discourage, identify, and report money-laundering. AML finds, freezes, and forfeits unlawful funds or assets. Money laundering is fought by identifying its causes. This variable measures customer awareness of AML, its tools, and their usage.

Know Your Customer (KYC) is a legal obligation to comply with Anti-Money Laundering (AML) rules. Effective KYC involves knowing a customer's genuine identity, financial activities, and economic risk.

*Reporting function:* Basel Committee issued ethical rules in 1988 to prevent banks from being used to launder illegal money and to discourage suspicious transactions. Transaction Suspicious (STR). A financial transaction is suspicious if there are strong reasons to suspect unlawful money or money laundering. From customer identification to transaction monitoring, the AML regime aims to detect and report suspicious money laundering and terrorism funding to the Financial Intelligence Unit. REs and bank personnel must recognize suspicious transactions. Only FIU should be notified about STRs. FIU decides whether a transaction is unlawful based on STR, as required by ALPA and related legislation.

AML/CFT: This section includes anti-money laundering policies, regulations, and law. Legislative and regulatory authorities adopted guiding principles to prevent terrorism and money laundering (Nobanee and Ellili, 2017). Assets Laundering Prevention Act, Mutual Legal Assistance

Act, Extradition Act, Organized Crimes Prevention Act, and Confiscation of Criminal Proceeds Act are used to measure Nepal's AML awareness.

Financial Information Unit of Nepal (FIU-Nepal) is a national AML agency. It gathers, processes, and shares information on money laundering, terrorism funding, and criminal proceeds. Nepal's central bank houses the independent FIU-Nepal. The Asset Laundering Prevention Act of 2008 established it as an administrative FIU on April 21, 2008. FIU-Nepal manages information sharing with abroad FIUs via the EGMONT network of FIUs and ensures domestic law enforcement agencies receive AML/CFT financial intelligence. Without international cooperation, globalization and liberalization can't prevent money laundering (Yasaka, 2017). FATF monitors money laundering globally. It's enacted 49 money-laundering standards. Money laundering is addressed in FATF 40. FATF 40+9 Special Recommendations on Terrorist Financing. All jurisdictions must follow these international norms. FATF includes Nepal.

The model of the study was adopted from the studies like Biswakarma and Koirala, (2021); Bahrin, Yusuf, Muhammad and Ghani (2022); and Viritha and Mariappan, (2016). Employees trainings and development regarding AML, Control over business sophistication, Business ethical behavior, Customer awareness on AML, and AML system are framed as independent variables, wherein the effective implementation of AML practices is considered as dependent variable in the study.

### III. Methodology

#### *Design, Population and sample*

The researcher used a quantitative research design to examine customer AML knowledge and the relationship between independent variables and effective implementation. Quantitative research is

used to test the study's hypothesis and investigate quantitative properties. The study uses causal research design to identify cause-and-effect links between independent and dependent variables. Out of total of 27 Commercial banks and 18 Development banks, the study comprises the response of customers from 35 banks. Previous study undertaken by Joshi and Shah (2020) assessed Customer awareness level on AML practices on 168 bank customers using convenient sampling method. This study's final sample consisted of 201 customers of the banks Kathmandu district assuming that the sample size of 200 is sufficient. The convenience sampling method, is used to choose the sample to accomplish the data collection within a stipulated time frame. Likewise, according to a banks supervision report by Nepal Rastra Bank as of July 2021, there are a total of 27 Commercial banks and 18 Development Banks in Nepal. Thus, the total population of the study is 45 banks. Due to the non-availability of employee count on the basis of department, the population of the study is assumed to be unknown. However, the researcher framed sample in such a way that the sample represents overall banks. Thus, the findings of the study are based upon the response from the employees from total of 35 banks (including Branch and Head office) out of 45 Banks. The study comprises the response of Operations In-charge, Branch Manager, and Compliance (AML/CFT Unit) team, a total of 200 employees were contacted, only 156 employees responded. The study of Vaithilingam and Nair (2007), Chisenga and Phiri (2011), Biswakarma and Koirala (2021) and Bahrin, Yusuf, Muhammad, and Ghani (2022) were based upon the sample size of 88, 62, 136 and 152 respectively. Thus, to examine the factors affecting effective implementation of AML practice, under this study the sample size of 156 is assumed to be sufficient.

### *Data Collection Tool-Instrumentation*

A structured, and self-administered questionnaire was used to collect the data. The study included closed-ended questions with a five-point agreement scale.

Study - I: For Bank ML/AML customer awareness, questionnaires was used. First section comprises respondents' gender, age, education level, and occupation. The second component of the questionnaire covers Customer ML and TF awareness. A total of 19 statements to capture awareness on the aspects: ML and its impact, Terrorism Financing, Bank as a channel of ML/TF activities, Customer identification norms and its importance, Reporting function, AML & CFT law, and FIU-Nepal. In this study, a Likert type five-point scale questionnaire was used to assess the customers' awareness level on ML/AML has been abstracted from the study of Viritha and Mariappan (2016).

Study – II: For Bank Employees' Perception structured questionnaire were used. Where the first section covers demographic information as gender of the respondents, type and location of the bank, and work experience of the respondents. The second section of the questionnaire consist of statements regarding the independent variable: Employee Training and Development adopted from the study of Bahrin, Yusuf, Muhammad, and Ghani (2022), Control over business sophistication adopted from the study of Bahrin, Yusuf, Muhammad, and Ghani (2022), Ethical Behavior adopted from the study of Viritha and Mariappan (2016), AML System adopted from the study of Viritha and Mariappan (2016) and customer awareness adopted from the study of Viritha and Mariappan (2016) . In this study, a Likert type five-point scale questionnaire was used to examine the impact of independent variables over dependent variable (Effective implementation of AML practices). The scale's five points ranges from 1 to 5: Strongly Disagree, Disagree, Neutral,

Agree, Strongly Agree. For the reliability analysis, the Cronbach's alpha was used. All the variables Cronbach's alpha is

greater than 0.7. Therefore, the scales are considered to be reliable and consistent to measure the respective variable.

**Table 1:** Reliability statistics of Bank Customer responses

Variables	No. of statements	Cronbach's Alpha
Money Laundering and its impact	5	0.86
Terrorism financing	2	0.61
Bank as a channel for ML/TF activities	2	0.81
Customer identification norms and its importance	4	0.72
Reporting function	2	0.88
AML & CFT law	2	0.79
Financial Information Unit	2	0.82

**Table 2:** Reliability statistics of employee response

Variables	No. of statements	Cronbach's Alpha
Employee training and development	6	0.796
Control over Business sophistication	8	0.743
Business Ethics	7	0.789
Customer Awareness	7	0.812
AML system	12	0.896
Effective Implementation of AML Practices	13	0.843

#### IV. Findings

##### *Demographic profile of the respondents*

Table 3 shows the demographics of bank clients and employees. A 201 bank clients were surveyed. Among 201 responders, 58.7% were female and 41.3% were male. A 65.2% of responders are 18-25, 33.8% are 26-40, and 1% are 41-60. Likewise, 52.2% of participants held a master's degree, followed by bachelor's and intermediate, 65.7% of respondents were students, 19.4% were private-sector employees, 10.4% were self-employed, and 4.5% were government employees. Similarly, the distribution of 156

employees by bank type are; most responders are from public banks (68.59%), followed by joint venture (18.59%) and government banks (12.82%). Respondent's employment roles. 48.72% of responses were from Compliance, followed by Branch Manager (26.28%), Operations in charge (18.58%), and Head Teller (3.21%). 91.02% of respondents have 3+ years of banking experience, 88.46% were from Kathmandu valley, and 11.53 % worked outside valley.

**Table 3:** Profile of the respondents -customers and employees

Customers profile		N	%	Bank employees' profile		N	%
Gender	Male	83	41.3	Type of bank	Public	107	68.59
	Female	118	58.7		Government	20	12.82
Age (years)	18-25	131	65.2		Joint Venture	29	18.59
	26-40	68	33.8	Position	Head Teller	5	3.21
	41-60	2	1		Operations in charge	29	18.58
Academic Qualification	Masters and above	105	52.2	Branch Manager	41	26.28	
	Bachelors	92	45.8	Compliance team	76	48.72	
	Intermediate	4	2	Others	5	3.21	
Occupation	Government Service	9	4.5	Experience	Less than 1 year	7	4.49
	Private Service	39	19.4		1-3 years	7	4.48
	Self-employed	21	10.4		More than 3 years	142	91.02
	Student	132	65.7	Location	Inside Kathmandu Valley	138	88.46
			Outside Kathmandu Valley		18	11.53	

### ***Bank Customers' awareness on ML/AML***

Nepalese bank customers are moderately aware of money laundering implications and anti-money laundering efforts. Nepalese bank clients were moderately aware of customer identification norms and their importance, money laundering and its impact, reporting function of BFIs, terrorism financing, bank as a channel for ML/TF activities, AML & CFT regulation, and Financial Information Unit. The survey indicated that bank consumers are aware of ML/AML activities considering all seven parameters utilized to determine customer awareness level. Based on bank customers' responses. This research also examined staff AML customer awareness. The result

reveals Nepalese bank customers' awareness of money laundering repercussions and anti-money laundering practices. As evidence that employees disagreed with customers being aware of ML/AML, the findings suggest that customers aren't aware (mean awareness level is less than 3 out of 5). Customers are aware that banks are used for ML/TF with a mean of 3.10. Customers are uninformed of money laundering, its consequences, client identification rules, and bank and FIU reporting functions. This survey indicated that Nepalese bank clients are moderately aware of ML and AML. The employees' view is different. According to bank personnel, customers don't know about ML and AML. A generic instrument

was created to measure customer awareness of ML/AML, KYC, AML/CFT legislation, and FIU-Nepal. To assess customers' awareness from workers' perspectives, the

instrument examines their support for KYC, information disclosure, etc.

**Table 4:** Bank Customers' awareness on ML/AML

Variables	Customer perspective		Bank employee perception on customers' awareness	
	Mean	Std. Deviation	Mean	Std. Deviation
Money Laundering and its impact	4.14	0.89	2.9	0.92
Terrorism financing	3.51	0.99	2.35	0.78
Bank as a channel for ML/TF activities	3.31	0.94	3.1	0.89
Customer identification norms and its importance	4.24	0.89	2.86	0.93
Reporting function	4.06	0.87	2.93	0.82
AML & CFT law	3.16	1.14	2.95	0.45
Financial Information Unit	3.12	1.11	2.56	0.82
Average	3.65	0.98	2.81	0.876

#### *Examine factors affecting effective implementation of AML practices*

The banks' AML practices were assessed on employee training and development, increasing business sophistication, business ethics, customer awareness, and the AML system. The Effective Implementation of AML Practices was evaluated using thirteen statements. On a five-point Likert scale, 1 indicated Strongly Disagree, 2 Disagree, 3 Neutral, 4 Agree, and 5 Strongly Agree about AML practices. The result indicates the highest mean of 4.10 for business ethics, indicating that Nepalese banks adhere to business ethics when upholding AML standards. Also at a moderate level of practice are employee training and development, business sophistication control, and the AML system. Nonetheless, client awareness appears to be lower, and employee responses are viewed as being lower. The moderate level of AML implementation in

Nepalese banks was indicated by a mean value of 3.53 (SD=0.497) for the overall application of AML practices, indicating moderate employee agreement. The result reveals respondents' level of agreement on AML training and development. There are 6 statements with mean values between 3.22 and 4.19, indicating that employees agree on the bank providing AML training and development. The highest mean 4.19 indicates that most respondents agree the bank conducts anti-money laundering training. Whereas. The mean 3.22 on the statement existing mechanism to monitor training & development connected to AML program is sufficient suggests that not most employees agree that the training measurement mechanism is insufficient.

The results also show whether respondents agree or disagree that company sophistication hinders AML implementation. The highest mean of 4.09 suggests banks have sufficient IT

infrastructure to track ML/TF transactions. The lowest mean indicates that most respondents believe electronic payment systems make it difficult to trace ML. The result demonstrates respondents' agreement with Business Ethics conceptions. Most respondents think that the bank is serious about reporting suspicious transactions to the FIU (4.37), followed by employees reporting suspicious transactions to supervisors (4.30) and the bank complying with relevant rules and regulations (4.20). (4.28). All statements mean a score above 4, indicating Bank is committed about ethical business. The employee disagreed with the premise that there is little pressure to develop a banking business at the cost of 3.42 compliance. The result demonstrates respondents' agreement on Nepalese bank customers' awareness of money laundering implications and anti-money laundering practices. Customers know less than 3 out of 5 about ML and AML practices. Customer awareness of the bank as ML/TF channel is 3.10 (mean).

Customers are uninformed of money laundering, its consequences, client identification rules, and bank and FIU reporting functions. Results also show respondents' agreement with AML system architecture. Each statement averages over 4/5. The mean score varies from 3.98 to 4.31, indicating that most respondents feel that banks' AML-related activities are carried out well. The implementation of the AML Practices seems to be moderately effective. Increased Business sophistication has not hindered in implementation of AML regimes has the lowest mean of 2.9 (SD=0.97) indicating the business sophistication has hindered the implementation of AML in a significant way. GOAML system software is used for reporting to FIU. Likewise, banking policy is directed towards conducting ethical business.

Further, table 5 exhibits the Skewness and Kurtosis test to the normality of the data. The results shows that the statistics lies between +3 to -3. This value is often compared to the normal distribution.

**Table 5:** Descriptive statistics of the variables

Variables	N	Mean	SD	Skewness		Kurtosis	
				Statistic	Std. Error	Statistic	Std. Error
Employee Training and Development	156	3.81	0.579	0.051	0.194	-0.45	0.386
Control over Business sophistication	156	3.43	0.526	0.016	0.194	-0.454	0.386
Business Ethics	156	4.10	0.504	-0.886	0.194	3.162	0.386
Customer awareness	156	2.86	0.613	0.312	0.194	0.113	0.386
AML System	156	3.83	0.420	0.127	0.194	-0.469	0.386
Effective Implementation of AML Practices	156	3.53	0.497	0.205	0.194	-0.376	0.386

### *Correlation analysis*

The correlation analysis result shows that there is positive correlation between all independent variables and between

dependent variables and independent variables. Pearson correlation ( $r=0.552$ ,  $p<0.01$ ) shows that there is a moderately positive relationship between training and development for employees and how

effectively AML practices are put into place. Also, the Pearson correlation of ( $r=0.689$ ,  $p<0.01$ ) shows that there is a high positive relationship between the sophistication of a business and how effectively AML practices are put into place. In the same way, the Pearson correlation ( $r=0.603$ ,  $p<0.01$ ) shows that there is a strong positive link between business ethics and the effective use of AML practices. Also, a Pearson correlation

of ( $r=0.610$ ,  $p<0.01$ ) shows that there is a high positive relationship between customers knowing about AML and how well AML practices are put into place. Also, Pearson correlation of ( $r=0.617$ ,  $p<0.05$ ) shows that there is a high positive relationship between AML system and effective implementation of AML practices.

**Table 6:** Correlation coefficient

Factors	Y
ET&D	.552** 0.001
COBS	.689** 0.001
BE	.603** 0.001
CA	.610** 0.001
AS	.617** 0.001

*N=156; Note. \*\* Correlation is significant at the 0.01 level (2-tailed)*

*Note: Where, Y= Effective implementation of AML practices; ET&D= Employees Training and Development; COBS= Control over Business sophistication; EB= Business Ethics; CA= Customer Awareness; AS= AML System*

### **Regression analysis**

To estimate the impact of the factors of effectiveness of the implementation of AML practices with the hypothesis was tested, and  $R^2$  was determined, using bootstrapping with 10000 subsamples using BCa bootstrap confidence intervals for significance testing with CI ranging from 2.5% to 97.5%. There was no change in the sign of the distribution (Hair et al., 2021). The Regression model depicts the R-square value is 0.677,  $F=62.857$ ,  $p=0.000$ , which means that the employee training and development, increased business sophistication, business ethics, customer awareness, and AML system account for

62.47 percent of the variation in the effectiveness of AML practices in Nepal's banking sector. Regression coefficients of 0.015, 0.289, 0.201, 0.242, and 0.290, respectively, are found for the five dimensions of the effectiveness of AML practices in Nepal's banking sector, which include employee training and development, control over business sophistication, business ethics, customer awareness, and AML system.

The regression equation for the efficiency of AML practices in Nepal's banking industry can be stated as:  $= -0.148 + 0.015ET\&D + 0.289COBS + 0.201BE + 0.242CA + 0.290AS$  based on the

coefficients. The outcome, however, demonstrates that the employee training and development dimension is insignificant

( $p > 0.05$ ) else all other factors are significant that impact on effectiveness of AML practices in banking sector of Nepal.

**Table 7:** Regression Analysis Estimates (with bootstrapping 10,000 sub sample)

	Coefficient	Bias	Std. Error	Sig. (2-tailed)	Bootstrapa	
					BCa 95% Confidence Interval	
					Lower	Upper
(Constant)	-0.148	-0.003	0.213	0.486	-0.557	0.264
Employee Training and Development	0.015	0.001	0.062	0.808	-0.106	0.142
Control over Business sophistication	0.289	-0.001	0.062	0	0.17	0.407
Business Ethics	0.201	0.005	0.064	0.002	0.095	0.349
Customer awareness	0.242	0	0.044	0	0.153	0.327
AML System	0.29	-0.004	0.083	0	0.122	0.44
R	.823a					
R Square	0.677				F	62.857
Adjusted R Square	0.666				Sig.	.000b

*Note: a. bootstrap results are based on 10000 bootstrap samples. Dependent Variable: Effective Implementation of AML Practices, b. Predictors: (Constant), AML System, Customer awareness, Employee Training and Development, Business Ethics, Control over Business sophistication*

As per the results, the hypotheses H2, H3, H4 and H5 have been accepted, which states that control over business sophistication, business ethics, customer awareness, and AML system has a significant positive impact on effective implementation of AML practices in Nepalese Banks. However, H1 has been rejected, which states that there is no impact of employee training and development in effective implementation of AML practices in Nepalese.

## V. Discussion

Money laundering can disrupt currency markets, global macroeconomic forecasts, and the financial system by creating illegitimate economies (Alexander, 2001). The international community has suggested

ways to combat money laundering to commercial and financial professionals and other responsible parties (Go & Benarkah, 2019). Nepal will comply with international money laundering norms and improve its legal and regulatory framework to fulfill its strategic gap action plan. Employee training and development (Biswakarma & Koirala 2021), control over business sophistication (Parashar, 2010), business ethics (Vaithilingam & Nair 2007), customer awareness (Viritha, 2016), and the anti-money laundering system (AML System) influence anti-money laundering practices, according to several studies (Bahrin, Yusuf, Muhammad, & Ghani 2022). Thus, anti-money laundering efforts are a major issue, and Nepal needs to analyze the barriers to AML



implementation. Anti-money laundering processes were examined in connection to employee training, business sophistication, ethics, and customer awareness. AML was considered. This study also examined bank staff and consumer AML awareness.

Bank consumers and staff were surveyed to determine their understanding. Nepalese bank clients understand money laundering and anti-money laundering, the study found. Employees saw the outcome as inconsistent. According to data, bank staff believe clients are unaware of money laundering and anti-money laundering. The analysis shows that employee and consumer perceptions of customer ML/AML awareness differ. The survey found that bank clients are extremely aware of ML/TF practices. Customers are aware of money laundering, reporting functions, customer identification requirements, and their importance compared to terrorism funding, banks as a route for money laundering and terrorist financing, AML and CFT legislation, and the National Reserve Bank's Financial Intelligence Unit. This study shows that clients are unaware of ML/AML procedures, contradicting Joshi and Shah's (2020) findings but supporting Viritha and Mariappan's (2016). According to Joshi and Shah (2020), providing thorough AML/CFT information during the KYC fill-out and account opening processes, on the bank's website, and via posters and display boards may boost customer awareness of AML policies. Joshi and Shah (2020) suggested that this may increase customer awareness of AML policies. The research also addressed why people are inexperienced with AML/CFT legislation. Nepalese laws change regularly, thus the Customer may not be aware of them. Without "civic education," Nepalese people lack basic awareness. The "Asset (Money) Laundering Prevention Act, 2008" is unknown to many, even though 65.2% of this study's participants held a bachelor's degree or higher. Customers have no idea what the FIU-NRB did. This research also examines the

obstacles to AML compliance in Nepal's banking sector.

Similarly, this study found that Control over Business sophistication, Business Ethics, Customer awareness, and the AML system all improve AML regulation implementation in Nepalese banks. Employee development, but not training, improves AML compliance in Nepalese banks. Most bank staff in this poll have received AML training. The other half receive training more than once a year. Bank employees have received enough ML/AML training, thus training and development do not affect AML standards implementation. The study supports and contradicts Vaithilingam and Nair's 2007 study, Parashar's 2010 study, Chisenga and Phiri's 2011 study, Viritha's 2016 study, Biswakarma and Koirala's 2021 study, Bahrin, Yusuf, Muhammad, and Ghani's 2022 study, and Viritha's 2016 study (2022). Strong courts and ethical banks minimize money laundering, according to Vaithilingam and Nair (2007). Parashar (2010) found that unethical firm behavior, financial market expertise, technology, and innovation strongly increase unlawful money flows.

However, business sophistication negatively impacts money flows and macroeconomic stability, and higher education and training do not appear to affect money laundering. Unlike Parashar (2010), Chisenga and Phiri (2011) found that AML requires training and strong internal controls. Viritha studied Indian banks in 2016 to see what factors affect AML implementation. Researchers found that AML training was inadequate, bank workers did not fully agree to follow AML processes, and banks only partially followed AML regulations. The survey found that lack of training and bank neglect of AML laws, standards, and processes were the biggest AML concerns. In 2021, Biswakarma and Koirala found that business sophistication control affects AML implementation the most. Employee

training and development do not affect AML implementation in Nepalese institutions. Researchers also recommended personnel training and development in anti-money laundering (AML), bank ethics, technical improvements, control over company complexity, and auditing and reporting standards to guarantee AML practices work. Bahrin, Yusuf, Muhammad, and Ghani (2022) found that staff knowledge and rules affect AML program performance. IT infrastructure hurts AML programs. Most bank employees believed that AML legislation, policies, bylaws, and procedures were taken seriously. Many bank employees believed the bank was committed to honesty. According to the findings, bank employees think the training and development program is sufficient. Employees agree that assessing training effectiveness is insufficient. Respondents agreed that company complexity made AML implementation harder. Most workers do not want customers to know about ML/AML and its effects. In a world where digitalization, such as digital currency and IT modernization, is accelerating, the bank and its staff should focus on improving their IT infrastructure and IT capabilities to detect and prevent suspicious actions. Nepal can better apply AML procedures if AML rules and practices aim to manage company difficulty.

AML policies must also examine the bank's morality. AML practices also need clients. Thus, Nepalese commercial banks should develop strategies to raise customer awareness and eliminate the gap between consumers and employees. These steps would help Nepal implement AML processes. Finally, each Nepalese bank follows the AML law and policy in its AML procedure. Implementation requires tight bank policies and regulations. Thus, bank front and back offices should be aware of general AML policies. Because the investigation found differences in bank staff AML knowledge. Thus, addressing

these inequalities can improve AML practices in Nepalese commercial banks.

## **VI. Conclusion**

Based on employee training and development, business sophistication, business ethics, customer awareness, and the AML framework, the study analyzed the AML practices of Nepalese banks. Additionally, the study reveals that the implementation of AML practices in Nepalese institutions is only moderately effective. The findings indicate that banks have adequate IT infrastructure to monitor ML/TF transactions and that banking policy is oriented toward ethical business practices. The study emphasizes the need for banks to increase customer awareness and develop more precise methods for measuring the efficacy of AML training and development programs. In Nepalese banks, employee development, but not training, enhances AML compliance.

Effective AML practices require personnel training and development in anti-money laundering, bank ethics, technical enhancements, control over company complexity, and auditing and reporting standards. Control over business sophistication is essential for the successful implementation of AML, meaning that control over business sophistication is one of the most influential factors in the effective implementation of AML practices in Nepalese banks. Overall, the study emphasizes the significance of anti-money laundering efforts and the need to continue analyzing the obstacles to AML implementation in Nepal's banking sector. It can be assumed that for AML implementation to work well, technological progress and the creation of a good IT infrastructure should be used. Finally, bank-level factors are essential for comprehending AML practices in banks. The success of AML practices can be influenced by organizational culture, leadership, technology, and governance

structures. Banks must prioritize these aspects and ensure that they have the resources necessary to comply with AML requirements and reduce risks.

From the point of view of bank employees, the study's results show that customers aren't very satisfactorily aware of AML practices. On the other hand, customers are very satisfactorily aware of AML practices. The study also found that Control over business sophistication, Ethical Behavior, Customer awareness, and the AML system all have a greater effect on how well AML practices are put into place. The results of the study will help the banks, the people who use the banks, and the people who make policy. There are differences in how much bank employees know about ML/AML practices based on which departments they work in. To be more specific, it seems like mid-level officers like the Operations In-Charge and Branch Manager know more and have been to more training and development programs than ground-level employees like front-line employees.

This study focuses on looking at the factors that affect how well AML practices are put into place from the point of view of mid-level employees (including Operations In-charge, Branch Manager and Compliance team). As such, an independent study with the same goal should be done with front-line employees who have direct experience with ML. Money laundering can also happen through finance companies, microfinance, cooperatives, and insurance, as well as commercial banks and development banks. Because of this, a similar study should be undertaken in different class of banking and financial institution in Nepal, which can be based on the minimum paid-up capital of a bank or financial institution and working areas in Nepal implement AML practices.

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