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## 11.4. Professionals: vulnerability of the auditors' sector

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### 11.4.1. General description of the sector

**Table 82.** Description of the auditors' sector

Market participants	Number of market participants as of 31.12.2019	Number of obliged entities	Existence of a professional association or umbrella organization
Auditors	130	100%	The Estonian Auditors' Association

Number of audit service providers as of 16.12.2020:

- 132 audit firms (hereinafter: AF) (1 license suspended) and 339 sworn auditors (hereinafter: SA), of which 121 do not provide audit services in AF. Thus, there are 471 obliged entities in the sector (AFs and SAs in total).
- All AFs and SAs are members of the Estonian Auditors' Association (hereinafter: EAA) due to the requirements of the Auditors Activities Act.

#### **Specificity of the Sector**

In the context of the Money Laundering and Terrorist Financing Prevention Act (hereinafter: MLTFPA), auditors are obliged entities primarily when providing audit services. When providing audit services, auditors do not participate in the client's transactions or mediate or advise on transactions. By performing an audit, they can see and check the data of customer transactions that have already taken place. In accordance with the requirements of the professional standards of auditing, the compliance of the data of major and significant client transactions with those reflected in the financial statements is verified in the course of auditing. The auditor does not check all the data of the client's transactions and does not perform 100% control over the data of the transactions. In fulfilling the requirements of the MLTFPA, the auditor can assist in the application of due diligence measures, including in determining the compliance of the data of actual beneficiaries and in notifying the Financial Intelligence Unit (hereinafter: FIU) of suspicious transactions and cash transactions exceeding 32,000 euros. In particular, the role of auditors is to be a necessary expert in identifying, verifying, and informing suspicious and unusual schemes in the auditee's business, as well as obtaining information on the auditee's compliance with the law.

#### **Legal framework**

- MLTFPA.
- Auditors Activities Act.
- Standards of professional activities for sworn auditors, in particular:
  - A code of ethics for professional accountants, which sets high ethical standards for the auditor, including independence requirements.
  - Quality control standard ISQC1.
  - ISA 240 Auditor's responsibilities for auditing financial statements due to fraud.
  - Compliance with ISA250 laws and regulations when auditing financial statements.
- Procedures of the Auditing Activities Oversight Council (hereinafter: AAOC):
  - Quality control procedures.
  - Disciplinary proceedings.
  - Complaints handling and investigation procedure.

- Guidelines of the Ministry of Finance (hereinafter: MoF) and the FIU.
- The EAA Guide to Rules of Procedure and Sample Paper Methodology for Customer Acceptance – a methodology that includes a customer acceptance questionnaire, including risk assessment questions and business relationship monitoring.

#### 11.4.2. Description of risk typologies

The auditor cannot be a participant in the money-laundering scheme. Auditors do not participate in or advise clients on possible money laundering schemes. Clients do not order an audit service in order to conceal the origin of the proceeds of crime. The auditor's work is aimed at auditing the client's financial statements, i.e., it is not possible to use his or her services for money laundering (it is not relevant in any of the classic stages of money laundering), nor is the service used for terrorist financing and brokering and distribution of weapons of mass destruction.

The auditor may contribute to the client's non-compliance with the MLTFPA, if he or she understands and identifies fraud, suspicious transactions, or the client's involvement in money laundering and terrorism, but fails to notify the client's management, law enforcement and FIU of the violation.

When performing an audit, the auditor may not detect all possible violations by the client, as the professional standards on the basis of which the auditor performs the audit do not provide for the obligation to verify the data of all client transactions. The auditor checks the compliance of the data of the client's significant and voluminous transactions with the financial statements. Due to the above, it may happen that the sworn auditor provides the client with an unqualified sworn auditor's report even if the client has not complied with the requirements of the MLTFPA and other laws.

In the framework of the survey, the auditors have also identified the following threats to money laundering transactions for customer transactions:

- Fictitious transactions are carried out (loans, non-existent services).
- Large cash transactions and cash withdrawals from the bank.
- Transactions concealing the beneficial owners.

#### 11.4.3. Threats

##### 11.4.3.1. Threats of money laundering

###### **The threat of cash transactions**

The threat is low:

- During the audit, the auditor examines the client's cash transactions in excess of 32,000 euros.
- Transactions broken down into smaller parts may go undetected.
- In the sectors where cash transactions take place – dealers, pawnshops, pursuant to § 91 and 92 of the Auditors Activities Act, undertakings do not have an audit obligation.

###### **Threat of failure to notify the client's management bodies, law enforcement agencies, and the FIU of suspicious transactions and fraud committed by the client and of discovery of violations of the requirements of MLTFPA and other laws**

The threat is low:

- The auditor is required to comply with the requirements of legislation and professional standards when providing the service.

- The auditor is responsible for violating the requirements of legislation, including the Auditors Activities Act and the MLTFPA, as well as professional standards.
- Compliance with auditing requirements is subject to thoroughly regulated and continuous periodic state supervision.
- Violation of legal and professional standards will result in sanctions.

**Conclusion**

**Table 83.** The threat level of money laundering in the auditor's sector

Sector	The threat level of money laundering at the sector level	
Auditors	1.45	<b>low</b>

The threat of money laundering in the auditors' sector is **low** both for cash transactions and for detecting suspicious transactions and frauds of the client and violations of the requirements of the MLTFPA in the case of failure to notify the client's management bodies, law enforcement agencies and the FIU.

**11.4.3.2. Threats of terrorist financing**

The threats of terrorist financing are similar for auditors to the threats of money laundering referred to in section 11.4.3.1.

**Conclusion**

**Table 84.** The level of terrorist financing threat in the auditors' sector

Sector	The threat level of terrorism at the sector level	
Auditors	1.4	<b>low</b>

The probability of the occurrence of terrorist financing in the economic transactions of the persons audited in Estonian society is estimated to be **low**.

**11.4.4. Vulnerabilities**

**11.4.4.1. Vulnerabilities of prevention of money laundering**

**11.4.4.1.1. Exposure to the threat**

- The threat of cash transactions: As the auditor controls client cash transactions in excess of 32,000 euros in all sectors except the merchant and pawnshop Sectors, the number of such transactions is small and can be adequately controlled. Also, in the case of larger cash transactions, the clients themselves are obliged to apply due diligence measures, which presumably means that the person related to the transaction has already been inspected by the obliged entity before reaching the auditor's desk.
- There is a theoretical threat of involving auditors in criminal schemes, but in the Estonian context, there is no data from recent years on cases of money laundering financing schemes that would

have taken place with the assistance of auditors.

Theoretically, the following could be considered vulnerabilities:

- The opacity of customer transactions.
- Failure to detect suspicious customer cash transactions and fraud exceeding 32,000 euros.
- Insufficient cooperation of auditors with obliged entities of MLTFPA in order to identify suspicious transactions.
- Insufficient feedback from FIU to auditors on compliance with the obligation to report suspicious transactions and use of information obtained.

The auditor does not control all transactions but works with the concept of materiality, so some transactions may go unnoticed.

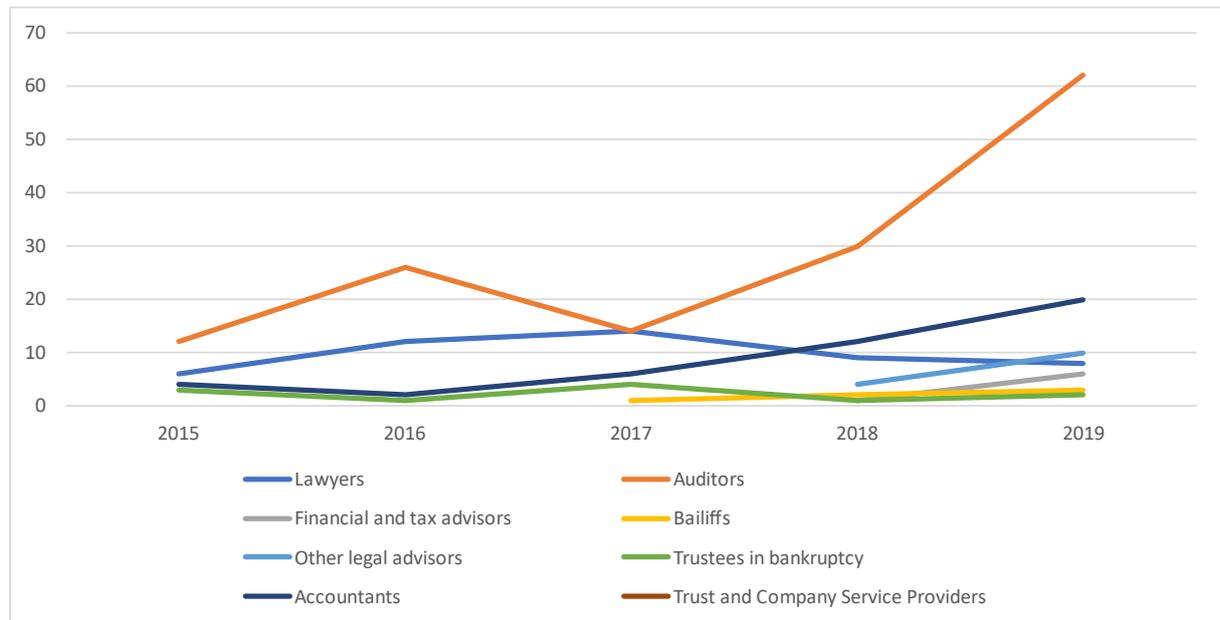
#### 11.4.4.1.2. Threat awareness

##### Management commitment and leadership

The results of the survey show that the sector's awareness of anti-money laundering is high, as evidenced by the number of notifications sent to the FIU. The reason for this can be considered the SA's compulsory in-service training obligation, the requirement to meet professional standards, the training provided by the EAA, and the guidelines prepared by the EAA on the rules of procedure and customer risk assessment.

The FIU's feedback given in 2019 to the consulting sector and public officials to the obliged entities shows that the frequency of notifications has increased. In particular, the **auditors** who submitted 62 reports in 2019 (2 STR; 7 UTR; 3 UAR; 49 CTR; 1 TFR) can be highlighted. The materials of the previous evaluation show that in 2012 a total of 17 amount-based notifications were sent by the auditors.

**Figure 26.** Statistics on the trend of reporting in the professionals' sector in 2015-2019



Source: Financial Intelligence Unit (FIU)

### 11.4.4.1.3. Legal framework and control

#### **Quality of supervision**

There is ongoing oversight in the sector – oversight by the FIU and the independent AAOC:

- The FIU supervises compliance with the requirements of the MLTFPA. In 2020, the FIU checked the compliance of several AFs with due diligence requirements.
- The FIU itself assesses that the quality of supervision is sufficient, but the frequency with which it is possible to carry out inspections of entities with a risk-based approach in the sector is insufficient.
- Independent AAOC – Auditors Activities Act and SA on compliance with professional standards:
  1. The intra-professional association quality control questionnaire approved by AAOC contains a number of questions on the requirements of the Auditors Activities Act, MLTFPA and professional standards regarding the measures taken by the SA to prevent money laundering and terrorist financing, including setting higher requirements for auditing. Mandatory continuous supervision – every 1–6 years depending on the experience of operating AF, the results of quality control, and the existence of a public interest entity in the customer base.
  2. AAOC has also performed special inspections by auditors on compliance with the requirements of the MLTFPA. There are no known violations of the requirements.

#### **Brief summary**

There is continuous state supervision in the sector by both the FIU and an independent supervisory body, the quality of supervision is sufficient, so the level of vulnerability is low.

#### **Effectiveness of compliance control systems and reporting**

Auditors mostly use questionnaires and analysis to achieve the objective. Questionnaires and analysis do not always require investment in technology, but about a third of AFs have done so. Public and private databases are also established to verify the data submitted by the customer, including personal data. Auditors do not have a regular reporting obligation to the FIU. The Oversight Board continuously monitors the quality of the auditors' audit work. In the course of supervision, the Oversight Board monitors the auditors' compliance with the professional standards and the requirements of the Auditors Activities Act as well as other laws. With regard to compliance checks, auditors are exempted from preparing a risk assessment document.

#### **Brief summary**

Compliance control systems and reporting are effective, so the level of vulnerability is low.

#### **Quality of the framework of due diligence measures applied with regard to customers**

The data provided by the customer is checked and compared with information obtained from a reliable source. Public and private databases are of help.

The strengths of SAs:

- EAA has developed guidelines for identifying client risks and drafting rules of procedure.
- EAA regularly organizes mandatory in-service training for auditors, including a cryptographic information day and a round table.
- As auditors have value in the national anti-money laundering system, in particular in the control of the transactions of persons subject to the audit obligation, unusual and suspicious transactions, or in the identification of schemes.

#### **Brief summary**

The quality of the customer due diligence framework is high, so the level of vulnerability is low.

**11.4.4.1.4. Sector-specific risk assessment with the quality of sector-specific controls**

There are no sector-specific vulnerabilities, as it is virtually impossible to use the sector's services for money laundering or terrorist financing – auditors do not transfer or hold values, nor are they parties to transactions.

A common problem is the data on PEPs and beneficial owners, which are not always available to international persons, which in turn makes it difficult to control transactions for money laundering in certain situations.

**11.4.4.1.5. Quality of response to risks identified in previous evaluations**

In its report for the third round of evaluations, MONEYVAL has highlighted the sector's shortcomings in general awareness of the issues of money laundering and terrorist financing. In order to eliminate the shortcomings, the EEA has continuously organized training to clarify and fulfill the requirements of the MLTFPA, also involving representatives of the FIU. Reporting activity to the FIU has increased strongly in recent years.

**11.4.4.1.6. Conclusion**

The vulnerability level of prevention of money laundering in the auditors' sector on a scale of 1–5 is 2.07, i.e., **low**.

**Table 85.** Level of vulnerability of prevention of money laundering in the auditor's sector

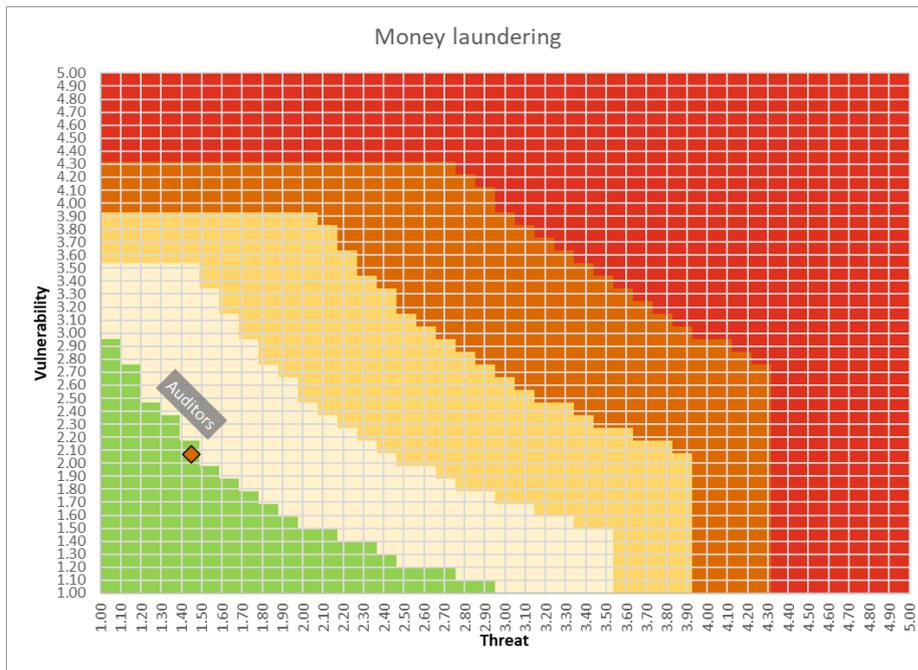
Sector	Level of money laundering vulnerability at the sector level	
Auditors	2.07	<b>low</b>

The strengths of the sector include a strong legal framework, mandatory in-service training for auditors, and mandatory in-house and public oversight. It should also be borne in mind that the purpose of auditing is to exercise control over the transactions of individuals ex-post, that is to say, after the transactions have taken place, and not to provide real-time services that could be used for money laundering or terrorist financing.

The weakness is access to information on beneficial owners and PEPs, in particular international information, which does not allow for the required level of due diligence.

Due to the low level of vulnerability of the sector, it is unlikely that there is a need to strengthen regulation or supervision of the sector for this reason, and the focus should be on maintaining the level achieved.

**Figure 27.** Heat map of the money laundering risk level in auditors' sector



**Summary**

The risk level of the sector in terms of money laundering is **low**, which means that the risk and its consequences must be accepted, and no specific measures are considered necessary. Simplified due diligence measures may be applied in the sector.

**11.4.4.1.7. Risk management strategy**

**11.4.4.1.7.1. Risk mitigation measures at the national level**

Based on the results of the risk assessment, the following suggestions are made to improve the situation at the national level:

- Making PEP data available to obliged entities.
- Establishment of a register of beneficial owners, which is currently being prepared by the MoF.
- The provisions of the MLTFPA concerning the application of due diligence measures, as well as compliance with the notification obligation due to the impossibility of applying due diligence measures, need to be reviewed. At present, the role of auditors as assessors of transactions that have already taken place in the national restraint system is to identify suspicions, the existence of an amount-based reporting obligation, and unusual transactions to report findings to the FIU, which will carry out further analysis. Due to the nature of the service, it is not reasonable to impose strict due diligence requirements (in particular identification and business relationship monitoring), which is also confirmed by the exemption from the obligation to prepare a risk assessment document under the MLTFPA.

**11.4.4.1.7.2. Risk mitigation measures at the level of obliged entities**

Based on the results of the risk assessment, the following proposals are made to improve the situation at the level of obliged entities:

- The Estonian Auditors' Association to continue conducting in-service training in the field of anti-money laundering, including the participation of FIU representatives with lecturers and the introduction of relevant legislation and guidelines for maintaining a consistently high level of auditors' awareness.
- Cooperation of the EAA with MoF and FIU to maintain a consistently high level of auditors' awareness.
- Exchange of information related to customers is important for meeting the requirements of the MLTFPA between obliged entities.
- Use of the database created by Credit Info in Estonia containing data on entrepreneurs, their representatives, actual beneficiaries, and PEPs.

#### **11.4.4.2. Vulnerabilities of prevention of terrorist financing**

Vulnerability of the prevention of terrorist financing in the auditor's sector is similar to the vulnerability of prevention of money laundering.

##### **11.4.4.2.1. Risk awareness**

###### **Management commitment and leadership**

The results of the survey show that the sector's awareness of the prevention of terrorist financing is average. The reason for this can be considered Estonian society, where the risk of terrorism is not high, and relevant training has not been conducted for obliged entities.

##### **11.4.4.2.2. Quality of terrorist financing detection and prevention of financing of proliferation of weapons of mass destruction**

###### **Quality of supervision**

High quality:

- High level of regulation - laws and special requirements in professional standards.
- A guide for assessing customer risks, including the assessment of geographical risks.
- Auditors have mandatory in-service training, which also covers the TF aspect.
- Mandatory internal and national supervision.

###### **Effectiveness of compliance control systems and reporting**

Auditors mostly use questionnaires and analysis to achieve the objective. Questionnaires and analyzes do not always require investment in technology, but about a third of AFs have done so. Public and private databases and public information are also used.

###### **Quality of the framework of due diligence measures applied with regard to customers**

The EAA has made available to the auditor's guidance material on the prevention of money laundering and terrorist financing, which is followed by control measures. The lack of data on terrorist organizations and international actors involved in terrorism can be a problem. Theoretically, it may be a case that the audited person may have performed some economic transaction for the purpose of the TF while applying the due diligence measures provided by the auditors for the MLTFPA, it is highly unlikely that the suspicion of the TF will be established.

###### **Quality of the identification of sector-based international sanctions**

The vast majority of auditors have not identified any cases where the audit client seeks to avoid taking restrictive measures that would otherwise have been required under the sanctioning legislation.

**11.4.4.2.3. Sector-specific risk assessment with the quality of sector-specific controls**

There are two ways to approach sector risks. Firstly, whether and how the supervisory audits have identified how the auditors' services are risks to perform operations or transactions for ML or TF purposes (i.e., how the audit service has been used to achieve the objective ML/TF), and secondly, whether such risks can be assessed through identified deficiencies. It is not viable that an audit service may be outsourced in any way to perform an ML/TF. The audit service still consists of providing an independent assessment so that the risks can be identified through shortcomings in the supervisory procedures carried out by the FIU. The main weaknesses identified by the FIU in the sector relate to compliance with the notification obligation (both the fulfillment of the notification obligation itself and the deficiencies in the internal procedures governing compliance with the notification obligation).

Thus, the sector-specific risks are low awareness or negligence in fulfilling the obligations imposed by law.

**11.4.4.2.4. Quality of response to risks identified in previous evaluations**

The results of the NRA 2015 showed that the level of vulnerability in the sector was low during the previous assessment period. It was recommended to focus on maintaining the achieved level while providing support for regular training in the prevention of money laundering and terrorist financing and for better cooperation between supervisory authorities in supervisory activities. These recommendations have been taken into account in the organization of audit activities, i.e., the situation has improved.

**11.4.4.2.5. Conclusion**

On a scale of 1–5, the vulnerability score for the auditors' sector in terms of terrorist financing is 2.00, or **low**.

**Table 86.** Level of vulnerability of prevention of terrorist financing in the auditor's sector

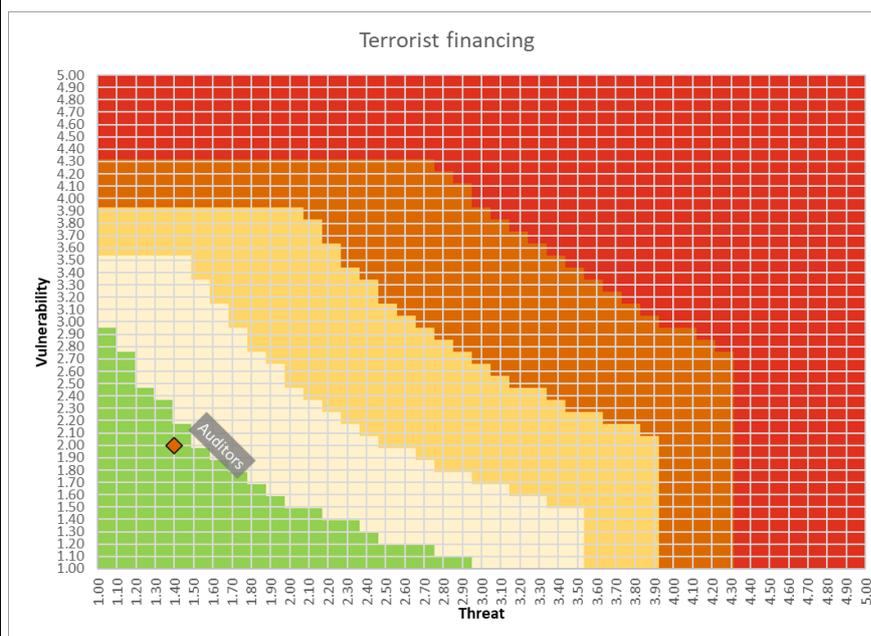
Sector	Level of vulnerability to terrorist financing at sectoral level	
Auditors	2.0	<b>low</b>

The strengths of the auditors' Sector can be considered to be the state and professional supervision performed by the FIU and the AAOC; a strong legal framework, in particular the requirements of the professional standards for auditors, the requirement for in-service training, and the existence of the EAA as a professional organization uniting and assisting auditors.

The most vulnerable places are the lack of information about foreign terrorist organizations and terrorists who have contact with Estonia. Access to information on beneficial foreign owners and PEPs has also been identified as a weakness.

Due to the low level of vulnerability of the TF sector, it is unlikely that there is a need for enhanced regulation or supervision of the sector for this reason, and the focus should be on maintaining the level achieved.

**Figure 28.** Heat map of the terrorist financing risk level of the auditors' sector



**Summary**

The level of risk in the sector in terms of terrorist financing is **low**, which means that the risk and its consequences must be accepted, and no specific action is considered necessary. Simplified due diligence measures may be applied in the sector.

**11.4.4.2.6. Risk management strategy**

**11.4.4.2.6.1. Risk mitigation measures at the national level**

Based on the results of the risk assessment, the following suggestions are made to improve the situation at the national level:

- Cooperation with and notification by the FIU and needs to be strengthened through the introduction of regular feedback obligations to the sector.
- To relieve the obligation of due diligence for auditors.

**11.4.4.2.6.2. Risk mitigation measures at the level of obliged entities**

Based on the results of the risk assessment, the following proposals are made to improve the situation within the Sector:

- To raise awareness through sector-specific training with the participation of FIU representatives.
- To provide market participants with a regular overview of typologies for auditing companies operating in different sectors, i.e., what to pay attention to when providing audit services.