TRANSPARENCY INTERNATIONAL
the global coalition against corruption

TOWARDS BETTER AML PRACTICE

ACCOUNTANCY SCOPING PAPER

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Transparency International EU's mission is to prevent and address corruption and promote integrity, transparency and accountability in the EU institutions and in EU internal and external policies, programmes and legislation.

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SCOPING PAPER

Transparency International is leading a three-year project **Toward Better AML Business Practices** (TBABP) aiming to improve the implementation and effectiveness of anti-money laundering (AML) standards and practices in selected sectors including the accountancy sector. Professionals such as accountants are at the fore front of the fight against money laundering playing an essential gatekeeping role in preventing, detecting and reporting suspicious activities. In particular, the accountancy profession, engaged in audit and tax advisory services, among other services, exercises a trusted oversight role in financial reporting and advising on tax payments.

Vulnerability of the sector to corruption and money laundering risks has been highlighted by the Financial Action Task Force (FATF). Similarly, risk assessments at both supranational and national level have identified significant risks to the sector. The profession itself recognizes the threats it faces and the obligations it has both in the public interest and to comply with AML legislation. Large global accountancy firms were signatures to the Professional Services Leaders' Statement at the London Anti-Corruption Summit in 2014, stating that[1]:

> *We strive to comply with all national laws and regulations combatting corruption and money laundering wherever we work and to apply the principles of a global approach when we work in those smaller markets where regulatory frameworks are less developed. We continue to develop our approach as we learn from experience, working on three fronts: systems, education and culture.*

This project aims to adopt the spirit of that statement when it said, "We now propose that our organisations work together to share experience, promote the codification of good practice, and in dialogue with government, regulators and professional bodies support their work addressing the practical limitations of the wider system we currently work within". Working with the profession and by leveraging its international partnerships networks, and expertise, through this project Transparency International will provide an external, independent and credible view on the issues.

The project objectives are to:

- Identify the challenges faced by the sector in implementing effective AML systems
- Identify, share and showcase best AML practices in the sector
- Strengthen the overall effectiveness of AML systems in the accountancy profession
- Raise awareness about AML standards and practices among professionals
- Provide guidance to professionals on how to implement effective AML systems
- Where issues of common interest are identified, advocate for policy change towards more effective AML standards

[1] Professional Services Leaders' Statement of Support for the London Anti-Corruption Summit 2014: http://www.ucl.ac.uk/news/news-articles/0516/statement_anti_corruption

This scoping paper considers the make-up of the profession and how the AML regime applies to it. It focuses on three main challenging areas for effective AML activity, including identification of risk, customer due diligence and suspicious transaction identification and reporting. It will inform discussion on the most significant challenges for the sector and how this project might approach them.

DEFINING THE SECTOR

One of the key difficulties in this area is defining the "accountancy sector", which is a catch-all term for a variety of different services offered by professionals with varying qualifications and experience. The term accountant is not "reserved" in all jurisdictions, so it can be problematic to identify all the firms and individuals who should be in scope of the AML regime. For example, in Germany the term 'accountant' has a legal meaning, but in the UK anyone can hold themselves out to be a so-called accountant, without any formal qualification or license.

Many accountants will be members of professional bodies, which are often also the relevant Self-Regulatory Bodies (including for anti-money laundering purposes), but there may also be an element of 'self-declaration', for example by professional bookkeepers. Recent experience in the UK is that even when such professionals approach statutory regulators for guidance, it is not always clear if they should be registered for anti-money laundering supervision.

The profession is made up of firms of very different sizes, from large global firms through to micro, small or medium size enterprises. The risks these firms face will also vary, as will the approach of supervisors to their regulation, although the services they offer are in principle the same. There are many millions of accountancy professionals globally – research by the International Federation of Accountants (IFAC)[2] in 2013 identified some 2.8 million members of professional bodies associated with IFAC and estimated that this number only represented around one third of those working in "accountancy related fields". Research carried out for the Consultative Committee of Accounting Bodies (CCAB) in the UK estimated that there were 22,000 accountancy firms in the UK alone, with the industry being "dominated" by the four large firms, each of which earned fee income of around £2 billion or more. The majority of the top 100 firms earned fee income of £15 million or less, indicating that the vast majority of firms are small scale in comparison[3]. The UK's National Risk Assessment of Money Laundering and Terrorist Financing (NRA) identified that 87% of accountancy services providers in the UK are sole traders or employ less than 10 people.[4]

The FATF approach

The accountancy profession is included in the 40 Recommendations[5] of the Financial Action Task Force (FATF), the global AML standard setter, as a so-called Designated Non-Financial Business and Profession (DNFBP). Accountants are therefore subject to the relevant preventive measures, including Customer Due Diligence (CDD) and record keeping. However, Recommendation 22

[2] Nexus 1: The Accountancy Profession, Behind the Numbers, IFAC 2013
[3] https://www.ccab.org.uk/documents/20170518TheAccountancyProfessionintheUK.pdf
[4] https://www.gov.uk/government/publications/national-risk-assessment-of-money-laundering-and-terrorist-financing-2017
[5] The FATF Recommendations, 2012: http://www.fatf-gafi.org/publications/fatfrecommendations/documents/fatf-recommendations.html

qualifies that only certain activity brings accountants within scope of the Recommendations (emphasis added):

> *22(d) Lawyers, notaries, other independent legal professionals and accountants* ***– when they prepare for or carry out transactions*** *for their client concerning the following activities:*
>
> - *buying and selling of real estate;*
> - *managing of client money, securities or other assets;*
> - *management of bank, savings or securities accounts;*
> - *organisation of contributions for the creation, operation or management of companies;*
> - *creation, operation or management of legal persons or arrangements, and buying and selling of business entities*

Recommendation 23 brings DFNBPs in scope of the Suspicious Transaction Reporting (STR) regime. This includes accountants when carrying out the activities listed above, but only when when "they engage in a **financial** transaction**"** on behalf of a client. This Recommendation also strongly encourages countries to extend the reporting requirement to "the rest of the professional activities of accountants, including auditing". In this context it is important to note that the FATF Glossary definition of accountants refers to "sole practitioners, partners or employed professionals within professional firms". It makes no attempt to define what "professional activities of accountants" might mean.

Application at EU level

The EU's 4th Anti-Money Laundering Directive (4MLD) transposes the FATF requirements into EU law.[6] It adopts a slightly different approach, by including the following definition as part of the list of obliged entities in Article 2 (emphasis added):

> "the following natural or legal persons acting in the **exercise of their professional activities**:
>
> (a) auditors, external accountants and tax advisors;"

This approach not only brings all the professional activities of certain sorts of accountants within scope of the reporting requirement, but also the CDD etc. provisions. It therefore represents an application of the AML regime to a wide range of firms and individuals, carrying out all their "professional activities". The list of specific services in the FATF Rec 22 does not appear in the Directive in relation to accountants (it does for lawyers). The Directive does not define the terms "auditors, external accountants and tax advisors". This leaves scope for significant interpretation at the national level.

Application at national level

UK example: The UK has a very large and diverse accountancy sector, which is largely self-regulated. It has implemented the requirements of 4MLD through the Money Laundering Regulations 2017, which include the following in the definition of relevant person (Regulation 2):

> "auditors, insolvency practitioners, external accountants and tax advisers"

Compared to 4MLD, insolvency practitioners have been specifically included in this definition, perhaps because it is a statutory function and specific risks have been identified relating to the termination of companies.. Again, there is no attempt in the Regulations to restrict the requirements to particular

[6] Directive EU) 2015/84, May 2015: http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=OJ:JOL_2015_141_R_0003&from=ES

sorts of activity, other than by the type of individual or firm involved. "External accountants" are defined as those providing accountancy services to other persons by way of business, but no definition is given of "accountancy services". National guidance from the CCAB limits this to "recording, review, analysis, calculation or reporting of financial information".

Application in other jurisdictions similarly varies according to the definition and supervision of the profession (indeed some jurisdictions, including the United States, have been reluctant to include accountants at all). For example, in **Germany** the AML law includes in the list of obliged entities (Section 2.1(8) of the Geldwäschegesetz) "auditors, chartered accountants, tax advisors and tax agents", a subtly different definition to the one adopted in the UK. It seems clear that although the FATF considers certain *activities* of accountants to represent the main risks, coverage of those activities in a supervisory and regulatory system constructed around *individuals and firms* results in some inconsistency.

There is also an issue around language and terminology. References to "the accountancy profession" or "accountants" may be inaccurate in relation to both the coverage of the sector and where risk is concentrated. A phrase such as "accountancy service providers" used in conjunction with a clear definition of which services are covered or regarded as high-risk could be considered. Many professionals, including those providing relevant accountancy services, intensely dislike being labelled "professional enablers" of crime. Whilst this may be an appropriate label for those who are complicit or negligent, its use does not foster good relationships between the competent authorities and the profession.

Questions for discussion:

Does the variance in national level application of the international AML standards relating to accountancy activity cause significant difficulty or create risks (e.g. of criminals targeting certain jurisdictions?)

Does the limited application of an AML regime to the profession, defined by activity or types of accountants, create confusion or difficulty? Or in practice are the obligations applied more generally across all the activities of accountants?

What are the practical challenges to an effective AML regime presented by the diverse make-up of the accountancy profession, for example the differences in business model and resources between the very large firms and SMEs, and how might these be overcome?

THE ROLE OF SUPERVISION

The roles of relevant statutory AML supervisors, accountants' professional bodies (which may or may not have self-regulatory roles in relation to AML, as well as wider professional standards) and the key AML agencies such as Financial Intelligence Units is key to effective implementation of the AML regime. The supervision of the accountancy sector is fragmented and organised differently in each jurisdiction. In particular, the sorts of services identified in the literature on money laundering risk may be offered by professionals in different types of firm, so a risk-based approach needs to cut across sector definitions, which are often reflected in supervisory structures.

There sometimes appears to be almost an adversarial relationship between the professional bodies and the authorities on this topic, inspired perhaps by a lack of mutual understanding and different

views on risk. Findings that the profession is "high risk" are often not quantified nor particularly well explained. Given the size of the sector, it is not realistic to approach the profession as if all accountants are potential criminals. A more collaborative approach to develop common approaches and understanding of risk, as is being advanced with the large banks in various jurisdictions through public-private sector partnerships, such as the UK's Joint Money Laundering Intelligence Taskforce (JMLIT), may mitigate this issue, but it is not clear what form such partnerships may take in the accountancy sector.

Questions for discussion:

What aspects of supervision of accountants are significant in establishing an effective AML regime and are there transferable elements of good practice?

Does the variance of approach internationally (particularly the roles of professional bodies in setting standards and the use of statutory supervisors) present practical challenges to international cooperation?

IDENTIFYING RISKS

We have seen above that the accountancy profession is generally brought into the AML regime and supervised on the basis of types of firms and individuals, even though the terms used (e.g. "accountancy services" are not necessarily clearly defined.

However, when reviewing literature on the risks posed by the profession, they are often defined by, or confined to, certain types of activity. There is a tension relating to a sectoral supervisory approach compared to activity-based risks. The international standards apply to certain types of activity (or all activity) carried out by professional services firms and individuals; Money laundering risks are concentrated in certain types of services carried out in relation to particular business activities.

For example, the EU's Supranational Risk Assessment (SNRA) deals with accountancy in various ways.[7] The sector as a whole is covered in 'Services from accountants, auditors, tax advisors', but references are found in various other sections, including:

- Creation of legal entities and legal arrangements
- Business activity of legal entities and legal arrangements
- Termination of legal entities and legal arrangements

The latter section identifies that:

> *Perpetrators may employ or require the services of accountants, auditors or tax advisors with a more or less level of involvement of the accountant, auditor or tax advisor himself with the aim to:*
>
> *- misuse client accounts,*

[7] European Commission, The Supranational Risk Assessment Report, June 2017: http://ec.europa.eu/newsroom/just/item-detail.cfm?item_id=81272

- purchase of real property,

- creation of trusts and companies/ management of trusts and companies,

- undertaking certain litigation, setting up and managing charities

- over or under-invoicing or false declaration around import/export goods.

- providing assurance

- tax compliance

They may be involved in ML schemes through the creation of 'opaque structures' defined as business structures where the true identity of the owner(s) of entities and arrangements in that structure is concealed through the use of, for example, nominee directors. The creation of such structure often set up in multiple jurisdictions including offshore centres is complicated and requires both regulatory and tax services of professionals.

This assessment, as can be expected at a supranational level, is quite general and non-specific in identifying how these risks present themselves in the professions. At a national level, more granular information may be provided, but even this is often regarded by members of the profession as either insufficiently detailed or to represent a misunderstanding of the scope and nature of accountancy services.

The recent UK NRA, for example, states that "accountancy services remain attractive to criminals due to their ability to use them to gain legitimacy, create corporate structures or transfer value". The analysis then refines this broad statement to suggest that specific services representing higher risk include company formation and termination; facilitating financial transactions (including use of client accounts); and tax evasion. This broadly agreesa with the SNRA, although different terms are used for the level of risk, without providing (in the public domain at least) detail of the evidence and analysis leading to this conclusion.

The profession itself has also considered the risks it faces and frequently disagrees with the characterisation of the sector as a whole as high risk, whilst not disagreeing with the premise that indeed accountancy services may be attractive to criminals and an important or integral part of some money laundering schemes. Industry guidance, such as the new CCAB Guidance for the Accountancy Profession[8], includes sections on the risk-based approach, consisting of consideration of how to carry out a risk assessment in accordance with the requirements and some discussion of 'risk factors'. However, the risk factors in Appendix E of the CCCAB guidance are not specifically tailored to the accountancy profession; they simply duplicate the generic list found in the Customer Due Diligence sections of the Money Laundering Regulations.

The Institute of Chartered Accountants of England and Wales (ICAEW), in a "Message to Members"[9], has highlighted the high-risk activities identified in the UK NRA and suggested that firms should use this information to further strengthen their AML procedures. It is left mostly to the individual firms to interpret how to apply this in light of their own business profile.

[8] http://www.ccab.org.uk/documents/TTCCABGuidance2017regsAugdraftforpublication.pdf
[9] http://www.icaew.com/en/technical/legal-and-regulatory/money-laundering/uk-law-and-guidance/nra-message-to-members

There is limited case history and research on the actual role of accountants in money laundering. Dr Katie Benson in her PhD thesis on the use of professionals in money laundering in the UK identified a lack of such evidence.[10] However, in her interviews with both professionals and law enforcement officers, risks were identified in small and non-chartered accountancy firms. There is also the question of complicity, negligence and ignorance – some money laundering schemes will require the involvement of professionals, simply because of the techniques used (such as complicated, cross-jurisdictional corporate structures). There is not much more than anecdotal evidence of involvement of corrupt professionals per se, either in the design of money laundering schemes or wilfully facilitating them.

The European Parliament's Panama Paper Committee recognised this issue and included in its recommendations a call for Member States to provide guidance on the risk factors arising from transactions involving tax advisors, auditors, external accountants, notaries and other independent legal professionals. [11]

This lack of an evidence-based and shared understanding of the roles, witting or unwitting, that accountancy professionals play in money laundering limits the effectiveness of the AML regime. Professionals giving advice or carrying out audits or other services typically do not handle client money, so may not see themselves as being vulnerable to "money laundering"; experience also shows that law enforcement may have unrealistically high expectations of the scope of professional audits, for example (by expecting accountants and auditors to have detailed knowledge of individual transactions being carried out by their clients as part of their 'know your customer' information).

Questions for discussion:

What more can be done by the authorities, AML supervisors and the profession itself to work together to assess the risks to the profession in a more detailed format?

What particular information will help those in the profession identify the specific risks they face in their practice and the mitigations they need to apply?

Are there other significant challenges to risk identification that the project should consider?

CUSTOMER DUE DILIGENCE

One of the obligations placed on accountants covered by the AML regime is customer due diligence (CDD). This should include both identification and verification of the client's identity (and any Beneficial Owners (BO), in the case of legal persons). There are well rehearsed issues with CDD generally, for all entities covered by the AML regime. These include availability of BO information, particularly in "secrecy jurisdictions"; the apparent ease with which serious and organised criminals can procure good quality false documentation; and logistical challenges in maintaining up-to-date information for a large customer base. These challenges apply equally to those accountants who have to carry out CDD.

[10] Katie Benson, *The Facilitation of Money Laundering by Legal and Financial Professionals* (University of Manchester, PhD thesis, 2016): https://www.escholar.manchester.ac.uk/item/?pid=uk-ac-man-scw:301608
[11] PANA Committee Final Report, http://www.europarl.europa.eu/cmsdata/134368/A8-0357_2017_EN.pdf

There are more specific challenges for accountancy services providers. An AML Benchmarking Survey carried out by the ICAEW in 2011 identified several issues, with a significant number of firms not carrying out their CDD standards to the level suggested in professional body guidance. Resourcing is always an issue in smaller firms, so the large number of smaller firms in the profession may impact on the quality of CDD. It is a challenge for both professional bodies and AML supervisors to ensure a 'level playing field' across all firms and individuals in the profession.

When it comes to the types of activity regarded as high-risk, often involving off-shore jurisdictions and the use of corporate structures, the challenges of BO and obtaining data from other jurisdictions are more acute. Applying a risk-based approach to CDD, by identifying such high-risk activity early and having good CDD and client take-on procedures in place are important for firms involved in such activity. Larger firms engaged in this type of business as a matter of course should be well equipped to fulfil their obligations, but vulnerabilities may lie elsewhere if smaller firms are targeted by criminals to carry out lucrative work. Aligning good practice and risk are fundamentally important for the profession.

In transaction-based work, accountants may not be the only professionals involved – there may be lawyers and banks acting too. Over-reliance on other professions to carry-out due diligence (whether or not formal third-party reliance is involved) may represent a vulnerability in such circumstances. Cultural barriers may also play a part – clients may now be used to quite intrusive diligence from their banks, but expect less from their professional advisors. There is also the issue of the interplay between data protection and privacy laws with CDD requirements, perhaps particularly in light of new more stringent requirements on both sides. Firms in the EU are having to cope with the introduction of the 4th Money Laundering Directive (and the impending revisions to it) and the General Data Protection Regulation at more or less the same time, as well as increased regulatory and public scrutiny on certain types of activity following the Panama and Paradise Papers affairs.

Other aspects of the client relationship may also be challenging. Retail banks generally provide a continuous service to their clients and have a large amount of transactional data to draw on to test and develop their understanding of the customer's business or activity. Accountants may in some circumstances have less frequent contact (e.g. preparing annual returns), which makes continuous monitoring more difficult. To an extent, accountants must rely on information provided by the client. A long-term relationship with a client can lead to assumed familiarity with their business, but identifying changes over time is an important part of CDD. On the other hand, some engagements may be very short term and relate to advice on only part of a wider picture, the totality of which the accountant has little visibility.

Questions for discussion:

Is there more that should be done by professional bodies, AML supervisors and other authorities to improve standards of CDD?

How can CDD be more closely aligned to ML risk in accountancy services?

Are there other significant KYC/CDD challenges for the accountancy profession not identified above that the project should consider?

SUSPICIOUS TRANSACTION REPORTING

Low volumes and poor quality (in the assessment of FIUs, at least) of suspicious transaction reporting are commonly described issues in the sector. For example, in the UK the accountancy sector only submits around 1% of all STRs, whilst in Germany it is reported that only single digit numbers of reports have been made by the whole profession: in the UK and the Netherlands accountants make hundreds of reports (although this represent small proportions of the whole). Although such statistics have to be treated with some care, as they depend to an extent on the particular legal nature of the reporting requirement and coverage of the sector, it is clear that within most jurisdictions STRs are dominated by the banks, with DNFBPs, including accountants making proportionally much fewer reports. In its findings, the Panama papers committee noted that it "Deplores the fact that the number of STRs made to FIUs by accountants is low and does not reflect the sector's exposure to money laundering risks".

Of course, there is no "right" number of reports and there has been little analysis looking at the level of reports compared to the number of transactions for example, or indeed consideration of what a transaction might mean in the accountancy sector. The recent Europol report looking at STR regimes found that the lack of harmonisation of reporting requirements and recording practices across Europe made "any comparison of the implementation and effectiveness of the EU anti-money laundering directives and the effectiveness of suspicious transaction reporting difficult, if not impossible." [12] One key issue is the interpretation and definition in law of "suspicion" – in some jurisdictions, such as the UK, this is a relatively low threshold (in the Netherlands, the test for reporting is an even lower measure of 'unusual'); by contrast in Germany, the test almost amounts to actual knowledge.

Reporting systems are often geared towards the major reporters, typically retail banks, and the design of the reporting system itself may create a disincentive to reporting by accountants, which frequently does not relate to a single or simple financial transaction (such as a bank transfer). The issue of professional privilege may also mitigate against higher reporting levels in some jurisdictions.

From the types of risk outlined above as the most significant in the activities of the profession, it seems likely that reports will be more narrative based and relate to an arrangement or corporate structures being operated by the client – this may fall better under a regime that considers suspicious activity as a whole, rather than transaction based reporting. Identifying and then reporting suspicions about this type of activity may be inherently more difficult than spotting an unusual transaction on a bank account. Simple red flags (such as use of secrecy jurisdictions or funds originating from "high-risk" countries) may not provide enough detail for accountants to spot truly suspicious activity and they would say that the general lack of feedback from FIUs on STRs makes it hard to refine their detection systems. The nature of the services offered by the sector means that the types of technological solution deployed by banks are unsuitable for use by the profession.

FIUs may find it hard to understand the suspicions being outlined in professionals' reporting, partly because the low number of reports may mean a lack of familiarity with how to present the information usefully on behalf of reporters. Equally, those in the profession suspect that there is a general lack of understanding in the competent authorities of their role and scope of their activities.

[12] 'From Suspicion to Action – Converting financial intelligence into greater operational impact', https://www.europol.europa.eu/newsroom/news/global-anti-money-laundering-framework-%E2%80%93-europol-report-reveals-poor-success-rate-and-offers-ways-to-improve

Questions for discussion:

What more can be done to facilitate identification of suspicious activity reporting in the profession, considering its diverse nature and the high-risk activities:

- **Are there sufficient meaningful "red flags" of suspicious activity and, if not, how can they be developed?**
- **Is training and supervision of the sector sufficiently focused on identifying suspicious activity, rather than compliance with legal and regulatory requirements?**

What measures can be taken by both reporters and FIUs to improve the quality and usefulness of reports made?

Are there other factors that impact on the quality and value of suspicious activity reporting by the profession?

CONCLUSION

There can be little doubt that some accountants, knowingly or unknowingly, and with varying degrees of complicity, are involved in money laundering. The make-up of the profession and the services it provides represent vulnerabilities that must be addressed by the global AML regime. Nonetheless, there are challenges in transposing the requirements of that regime, which were originally conceived for the banking sector, into professional services and various factors unique to the accountancy profession present specific difficulties.

By adopting a public-private partnership to better understand and address the risks, a more effective AML regime can be embedded in the accountancy services sector. Similarly, the many different national and international accountancy bodies have a role in ensuring that AML activity is a core part of the ethical and professional approach of accountants. This project will seek to facilitate such progress and enhance the role of accountants at the forefront of the fight against money laundering.

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