

NJORD Estonia: Peek to AML Risks and Red Flags of the Estonian Crypto Exchanges

Starting from 10.03.2020, virtual currency service providers^[1] are treated as 'Financial Institutions' in Estonia and are obliged to the same AML/KYC requirements as the financial institutions.

[1] Virtual Currency Service provider includes virtual currency wallet services providers and virtual currency exchange service providers.



Since bitcoin was launched in 2009, different cryptocurrencies have been moving at lightning speed in the financial world. The crypto exchanges are growing day by day and as of writing this article, there are around 250 licensed crypto exchanges in Estonia. Even the most conservative banks in the world are now welcoming crypto assets. In the Estonian context, to be precise, LHV bank seems to be a forerunner by onboarding virtual currency service providers.

AML Risks of Crypto Exchanges and Wallet Service Providers

Crypto exchanges are overnight becoming important in the financial systems and therefore also subject to criminal activities. Criminals are trying to take advantage of the system's shortcomings. Since crypto exchanges and cryptocurrencies are a new market compared to the traditional financial market, they have many system gaps and are therefore more vulnerable to money laundering risks than other financial systems. AML risks in crypto exchanges are related to new technologies and incompetent understanding of how technology imposes such risk. Here, experienced lawyers collaborating with developers can actually make a huge difference to prevent such AML risks.

Most common risks related to virtual currency service providers are the anonymity of transactions made on such exchange, security vulnerabilities in the systems, malicious software and the use of illegal goods and services to pay for terrorist finances. Some of the risks are inherited and some of the risks are controllable.

Crypto Exchanges AML Red Flags

In Estonia, the Financial Intelligence Unit (FIU) conducts supervision over crypto exchanges and wallet service providers, but as the cryptocurrencies are so popular, virtual currency service providers are struggling with AML risks. In 2020, the FIU has been very active on screening and mapping AML Red Flags and revoking issued licenses. The report prepared by the Financial Action Task (FATF) in 2020 aims to help virtual currency service providers to develop AML programs. NJORD Law Firm is actively monitoring these developments and has helped several companies to improve or develop an AML program that meets the new rules and complies with FIU's interpretation.

FIU is aware of the money laundering risks in crypto exchanges, and as this industry develops, regulators increase their regulations. To successfully apply for a virtual currency exchange license in Estonia or maintain the already received license, the service provider has to improve its AML risk procedures and models continuously.



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