

IESBA Exposure Draft, *Responding to a Suspected Illegal Act*—

Summary of Significant Comments on Exposure and Preliminary Task Force Analysis of Significant Issues

I. Overview of Responses

1. The comment period for the exposure draft (ED) of the proposed changes to the *Code of Ethics for Professional Accountants* (the Code) addressing a professional accountant's (PA) response to a suspected illegal act (SIA) closed on December 15, 2012. Comment letters were received from 73 respondents. This is a substantially higher response rate than on previous IESBA projects, clearly highlighting the importance of, and level of interest in, the topic addressed by this project. A listing of those respondents is provided in Appendix 1.
2. The table below paints broadly the balance of *overall* support for the proposed changes to the Code.

Category of Respondent	Overall Support?			
	Yes	Part Support/ Concerns	No	Total
IFAC Member Bodies ¹	7	3	23	33
Firms			12	12
Regulators and Public Authorities	1	3	1	5
National Standard Setters			2	2
Other Professional organizations		4	15	19
Individuals & Others	1		1	2
Total	9	10	54	73

3. As is apparent from the relative weight of overall support above, there has been a high level of opposition to the ED across all the main categories of respondents, except regulators and public authorities. The key themes from the responses are highlighted below.

KEY THEMES FROM RESPONSES

4. Overall, there has been general support for the IESBA to explore appropriate responses by PAs to SIAs in the public interest. Respondents from the regulatory community,² in particular, were

¹ Certain IFAC Member Bodies also hold the dual role of ethics standard setter in their jurisdictions.

supportive of the IESBA's efforts to provide better guidance not just to auditors but also to PAs in public practice providing services to non-assurance clients and PAs in business (PAIBs) in considering appropriate responses to SIAs they might encounter when carrying out their engagement or employment responsibilities, as appropriate.

5. However, there has been substantial push-back from other respondents against the three main proposals in the ED, i.e.:
 - The requirement to disclose certain SIAs to an appropriate authority if the entity has not self-reported;
 - The requirement to disclose certain SIAs to the external auditor in specific circumstances; and
 - The right to disclose certain SIAs to an appropriate authority in specific circumstances and the expectation that such a right would be exercised.
6. In this regard, respondents expressed fundamental concerns about the proposed requirement for PAs providing professional services to an audit client to disclose certain SIAs to an appropriate authority in the absence of a legal or regulatory framework that requires such a disclosure and in the absence of appropriate legal protections. Many³ felt that establishing a requirement to disclose to an appropriate authority falls within the remit of national legislators rather than a code of ethics. However, several respondents⁴ thought that the IESBA and IFAC should engage with governments and regulators directly or through the G20 and IOSCO to explore global principles and stimulate appropriate changes in laws and regulations.
7. Other respondents felt that the IESBA had strayed beyond the original objective of the project to provide guidance to PAs in responding to SIAs. Some⁵ in fact suggested that the IESBA learn about the experiences of countries that have implemented laws and regulations dealing with whistle-blowing before trying to introduce a requirement to report to an appropriate authority. Perhaps summing up the overall sentiment, a regulatory respondent,⁶ while supporting the IESBA's efforts in undertaking this project, felt that the pendulum had swung too far away from PAs' existing duty of confidentiality.
8. Respondents also expressed substantial concerns about the proposed requirement for other professional accountants to disclose certain SIAs to the external auditor, believing that it would inappropriately alter, and unreasonably extend, the role and responsibilities of auditors. Many also fundamentally objected to the proposed right with the expectation to disclose, believing that in practice such a construct would be indistinguishable from an obligation.

² 7AR, FRC, IOSCO

³ Regulators: FAOA, IRBA; member bodies: ACCA, AICPA, CAI, CICA, CNCC, CPAA, FAR, FSR, IBR, ICAEW, ICAP, ICAS, ICJCE, IDW, JICPA, KICPA, MIA; firms: BDO, DTT, EYG, KPMG, Kreston, MG, PwC; other organizations: APPC, CARB, CCAB, FEE, NASBA, NZAASB, PICPA, SRA, USCC

⁴ Member bodies: CAI, CNCC, ICAS, ICJCE, NBA; firms: EYG, KPMG; other organizations: CCAB, FEE

⁵ Member bodies: ICAP, JICPA, WPK; firms: DTT, MNP, PwC

⁶ IOSCO

9. Many significant concerns were also expressed about the complexities involved in, and the practicalities of, applying the main proposed requirements. Many therefore believed that these requirements would be unworkable.
10. Further, respondents raised significant concerns about the potentially complex interactions of the proposals with national laws and regulations⁷ and the related implications in cross-border situations.⁸ It was pointed out that it may be difficult in some circumstances to establish which of the Code or national requirements would be more stringent with respect to disclosure. It was also noted that there could be many layers of confidentiality (such as ethical, data protection, banking secrecy, and legal privilege) and different implications of breaching these.
11. Significant concerns were also raised about the interactions of the proposals with the ISAs and the related implications for the ISAs.
12. Respondents also raised fundamental concerns about the use of the public interest threshold for determining whether a SIA should be reported to an appropriate authority, with many believing that such a threshold would not be capable of being applied consistently without a definition of, or further guidance about, the concept of the public interest in the context of the Code.
13. Despite the fundamental concerns above, a view appears to have coalesced among many⁹ respondents that a possible way forward could be to do away with the main requirement to report to an appropriate authority and, instead, explore appropriate circumstances in which PAs could be *permitted* to override confidentiality and disclose SIAs to an appropriate authority.
14. With respect to the suite of 18 questions in the ED, responses to many of them were varied and highly nuanced, reflecting the complexity of the issues in this project.

TO CONTINUE OR NOT TO CONTINUE?

15. Given the high level of opposition to the ED, the Task Force felt it important to determine whether there is a critical mass of respondents who have called for the IESBA to abandon the project. From the Task Force's analysis of the responses, it appears that only a small minority of respondents¹⁰ have explicitly indicated that the topic should be addressed in law or regulation and not in an international code of ethics. The overwhelming majority of the respondents, while often harboring significant – and at times fundamental – concerns about various aspects of the proposals, did not indicate that they do not support the project.
16. Indeed, among those who can be characterized as not in overall support of the ED as it currently stands, many have nevertheless expressed support for various aspects of the proposals or offered suggestions for alternative pathways that they felt could overcome many of the practical difficulties associated with the proposals. Importantly, none of the regulatory respondents has expressed the view that the IESBA should no longer pursue the project.

⁷ Member bodies: ACCA, AICPA, CICA, CNCC, FSR, ICAEW, ICAP, ICAS, KICPA; firms: BDO, EYG, Mazars, MG, PKF, PwC; other organizations: CCAB, IIA, NASBA, USCC

⁸ Member bodies: CPAA, ICAEW, ICJCE, KICPA; firms: DTT, Mazars, PKF, PwC; other organizations: APESB, FEE, IIA

⁹ Member bodies: CAI, CPAA, CIMA, ICAA, ICAEW, ICPAC; firms: EYG, GT, Mazars, PKF; other organizations: APESB, CARB, GLW, PICPA, SMPC

¹⁰ Member bodies: CNCC, FAR, FSR, IBR, ICAS, ICJCE, IDW, KICPA, MIA, WPK; other organization: FEE

Matter for Consideration

Do IESBA members agree that there is sufficient overall support from respondents for the Board to continue with the project?

STRUCTURE OF PAPER

17. Respondents' significant comments are summarized below. At this stage, the Task Force has undertaken only a preliminary analysis of the issues and only tentatively explored a possible way forward. The Task Force anticipates developing firmer proposals for the IESBA's consideration at the June 2013 meeting, taking into account the Board's views on the significant issues presented below.
18. This paper is structured as follows:
 - I. Overview of responses
 - II. Pivotal issues
 - A. Disclosure to an appropriate authority
 - B. Disclosure to the external auditor
 - C. Right with expectation to disclose to an appropriate authority
 - III. Secondary issues
 - D. The public interest test and the escalation threshold
 - E. Requirement to confirm or dispel the suspicion
 - F. Meaning of key terms
 - G. Types of SIAs to be disclosed
 - H. Interaction of the proposed standard with ISAs
 - IV. Other issues
 - I. The exception provision
 - J. Scope of application of the proposed standard
 - K. Documentation

Appendix 1: List of respondents

Appendix 2: Exploring a way forward

II. Pivotal Issues

19. The IESBA is asked to consider the three pivotal issues below and share reactions to respondents' significant comments on those issues as well as the Task Force's exploratory thinking on a possible way forward as outlined in Appendix 2.

A. DISCLOSURE TO AN APPROPRIATE AUTHORITY

20. The ED proposed that a PA providing professional services to an audit client be required to disclose certain SIAs to an appropriate authority after having gone through the full process of discussing the SIAs with management or those charged with governance (TCWG) and concluded that the entity has not self-reported, and after having determined that the SIAs are of such consequence that disclosure would be in the public interest.
21. A small minority of respondents¹¹ were generally supportive of the proposal.
22. A significant majority of the respondents, however, were opposed to, or had major or fundamental concerns about, the proposal. In particular, a regulatory respondent¹² was of the view that the ED “seems to swing the pendulum quite far away from (the auditor’s) existing obligation of confidentiality.” The respondent felt that this was because the ED proposed that, “except in the case of anticipated bodily harm, auditors should report to regulators those SIAs that management does not itself report, regardless of whether the auditors’ expertise and work have a nexus to the regulators and without regard to the regulators’ means to intake (or) process (the reports of the SIAs,) or carry out related enforcement.”
23. Opposition to the proposal also came on many other significant grounds, including the following:
- It would be unfair, inappropriate or disproportionate to require disclosure in a global Code without legal protections, a prerequisite to whistle-blowing. In particular, it was noted that the Organization for Economic Cooperation and Development (OECD) has recommended its member countries to consider requiring auditors to report suspected acts of bribery to an appropriate authority but, at the same time, ensuring that protective mechanisms are in place.¹³
 - The Code cannot provide whistle-blower protection and so it would expose PAs to untenable personal and firm risk for both reporting and failing to report to an appropriate authority. It was felt that the IESBA would be acting beyond its remit in using the Code as a vehicle or legal instrument to establish such a requirement, and that the Code cannot be effective in doing so. It was noted that the proposed obligation has more of the characteristics of a legal requirement than a behavioral ethical issue and that it would be moving the Code away from a principles-based approach to addressing more legalistic questions of scope and definition. It was also argued that the matter should be addressed by legislators and regulators as they are able to provide necessary legal protections, consider measures that should be applied by all professions equally in responding to SIAs, and take the context of national legal and regulatory regimes into account.¹⁴

¹¹ Member bodies: CICPA, CNDCEC, ICPAC, ICPAK, ICPAR, ICPAU, ZICA; other organization: IIA; others: DE

¹² IOSCO

¹³ Member bodies: ACCA, CAI, CICA, CPAA, FSR, HKICPA, ICAA, ICAS, MIA, NBA, SAICA, WPK; firms: BDO, DTT, EYGG, GT, PKF, PwC, RSM; other organizations: AAA, APESB, APPC, Assirevi, CalCPA-CPC, CARB, FEE, NZAASB, SMPC, USCC

¹⁴ Regulators: FAOA, IRBA; member bodies: ACCA, AICPA, CAI, CICA, CNCC, CPAA, FAR, FSR, IBR, ICAEW, ICAP, ICAS, ICJCE, IDW, JICPA, KICPA, MIA; firms: BDO, DTT, EYG, KPMG, Kreston, MG, PwC; other organizations: APPC, CARB, CCAB, FEE, NASBA, NZAASB, PICPA, SRA, USCC

- The reporting obligation should rest with management and TCWG,¹⁵ and appropriate consideration should be given to their roles.
- The proposal would significantly impact the PA's relationship with the client or employer, turning the PA into a policeman or informant and promoting mistrust.¹⁶ In the context of audit engagements, this in turn could have a chilling effect by reducing the free flow of information from clients, thereby adversely impacting audit quality.¹⁷
- The proposal, and the supporting requirements, could significantly broaden the scope, and therefore cost of, the audit, or turn the audit into a forensic audit.¹⁸ It was also noted that there could be an increase in the expectations gap regarding what an audit is expected to achieve.¹⁹
- It would also place significant or disproportionate burdens on PAs and firms (particularly SMPs), such as in terms of the adverse impacts on cost and availability of additional liability insurance. Further, such additional costs may not be recoverable.²⁰
- The proposal could have a number of other unintended consequences, including:
 - Discouraging entities from engaging PAs in favor of other professionals not subject to the same Code.²¹
 - Creating turmoil in the capital markets and potentially harming companies, their employees and shareholders as a result of the disclosure of wrong information.²²
- The proposal could expose PAs to severe consequences if the SIAs are proven to be not illegal and no safe harbors are available. Such consequences would include: significant legal liability through defamation litigation or otherwise, reputational damage, and jeopardizing the PA's career.²³
- It would create an uneven field where there are no requirements comparable to this and other proposals in the ED for other accountants, lawyers and other professionals.²⁴
- It could lead to dueling professional standards where the PA is also a member of another profession that prohibits confidentiality overrides (e.g., if the PA is also a lawyer).²⁵

¹⁵ Member bodies: AICPA, ICAEW, WPK; firms: DTT, KPMG, MG, PwC, RSM; other organizations: Czech, USCC

¹⁶ Member bodies: ACCA, CGA, CICA, ICAP, HKICPA, IBR, ICAA, MIA; firms: BDO, DTT, PwC, RSM; other organizations: APESB, CCAB, EFAA, PICPA, USCC

¹⁷ Member bodies: AICPA, CICA, FSR, ICAEW, MIA, WPK; firms: BDO, DTT, Mazars, MG, PwC, RSM; other organizations: CalCPA-CPC, CARB, Czech, FEE, NASBA

¹⁸ Member bodies: IDW, KICPA; firms: MNP, PwC; other organization: NZAASB

¹⁹ Member bodies: CGA, IDW; firm: PwC

²⁰ Member Bodies: CICA, FSR, ICAP, IDW, KICPA, WPK; firms: MG, MNP, PwC, RSM; other organizations: EFAA, NZAASB, SMPC

²¹ Member bodies: AICPA, ICAEW, ICAP, IDW; firms: BDO, KPMG, PwC; other organizations: APESB, Assirevi, SMPC

²² Member Body: KICPA; firm: PwC

²³ Member Bodies: ACCA, AICPA, CIMA, CNCC, FAR, ICAEW, ICAA, IDW, JICPA, KICPA, SAICA, WPK; firms: MG, PKF, PwC; other organizations: APESB, APPC, Assirevi, CalCPA-CPC, IIA, IMA, NZAASB, PICPA, SMPC

²⁴ Member bodies: CNCC, FSR, HKICPA, ICJCE, MIA; firm: Mazars; other organization: FEE

- It would be incompatible with forensic accounting or expert witness services, which are often under attorney-client privilege, or due diligence services. Accordingly, PAs would be prevented from providing these services or companies may be discouraged from commissioning such services from PAs.²⁶

Respondents' Alternative Suggestions

24. Respondents provided a variety of suggestions for alternative approaches to a disclosure requirement in the Code, including the following.
25. Many respondents²⁷ were supportive of exploring a right or an encouragement, but not an obligation, to disclose to an appropriate authority, although a few of them felt that legal protections should still be in place and that there should be no breach of confidentiality under the Code.
26. Several other respondents²⁸ suggested exploring guidance on actions PAs should consider taking when a SIA is identified, but not requirements.
27. A regulatory respondent²⁹ called for "the proper balance with respect to what the audit firm is both called upon and allowed to do under the Code and/or the ISAs in handling the various scenarios involving SIAs." In particular, the respondent suggested that the IESBA's re-deliberations address the following, amongst other matters:
 - Establishing whether the project should encompass both SIAs that a PA encounters while the act is being planned and those that are identified after the act has occurred.
 - As PAIBs are the first line of defense, re-deliberating the Code's expectations for what they should do when they encounter SIAs.
 - Coordinating with the IAASB with respect to a review of how the existence of a SIA at an audit client affects the auditor's work on the financial statement audit, and establishing what incremental steps the external auditor is called to take beyond those called for by the ISAs.
28. A few respondents³⁰ suggested providing guidance to PAs on what not to do when faced with a SIA, for example, not assisting clients or employers in committing illegal acts, not turning a blind eye to the acts, and not resigning from audit engagements without explanation. A few others³¹ suggested that using hotlines or other whistle-blowing protections may be an appropriate means for some PAs to discharge their duty to respond.
29. In addition, a few³² suggested limiting the proposals to auditors only.

²⁵ Member body: ICAEW; firms: BDO, DTT, KPMG; other organization: Assirevi

²⁶ Member bodies: AICPA, CICPA, ICAEW; firms: BDO, DTT, EYG, GT, KPMG, PwC; other organization: Assirevi

²⁷ Member bodies: CAI, CPAA, CIMA, ICAA, ICAEW, ICPAC; firms: EYG, GT, Mazars, PKF; other organizations: APESB, CARB, GLW, PICPA, SMPC

²⁸ Member bodies: AICPA, CGA, CPAA, ICAA; firms: KPMG, GT, Mazars; other organization: CARB

²⁹ IOSCO

³⁰ Member body: ICAEW; firm: PwC

³¹ Member body: NBA; other organization: NASBA

³² Member body: JICPA; firm: EYG

Matter for Consideration

IESBA members are asked for view on, and reactions to, respondents' comments and suggestions above. In particular, given the level of opposition and concerns expressed by respondents, does the IESBA agree that it would not be appropriate to pursue further the proposal to establish a requirement to disclose to an appropriate authority? What are IESBA members' views as to what the alternatives might be?

B. DISCLOSURE TO THE EXTERNAL AUDITOR

30. The ED proposed that a PA providing non-audit services to a non-audit client and a PAIB should disclose certain SIAs to the entity's external auditor, if any, after having gone through the full process of discussing the SIAs with management or TCWG and concluded that the entity has not self-reported, and after having determined that the SIAs are of such consequence that disclosure would be in the public interest. The explanatory memorandum to the ED asked respondents whether they agreed with the proposal in the context of both PAs providing services to non-audit clients and PAIBs.
31. Broadly, respondents' reactions to this proposal have been negative, although this has been somewhat counter-balanced by a number of suggestions for alternative approaches.
32. While a minority of respondents³³ were supportive of the proposal, a significant majority³⁴ was opposed to, or had significant concerns about, the proposal on diverse grounds, including the following:
- The proposal could only be supported if it were not contrary to legal or contractual confidentiality provisions, or the PA is not acting in a fiduciary capacity.³⁵
 - The auditor does not have a responsibility to act as a receiver and manager of SIAs for the entity. It is not the role of auditors to investigate all illegal acts, including those not related to the audit..³⁶
 - It would unreasonably extend the auditor's responsibility to acting on second-hand information revealed by others outside the firm and at any time.³⁷
 - Not all entities have auditors. Accordingly, there would be potential for inconsistent treatment.³⁸
 - It is unclear what the auditor would be expected to do with the information.³⁹

³³ Member bodies: CGA, CICPA, CNDCEC, ICPAC, ICPAK, ICPAR, ICPAU, ZICA; other organization: AAA (but only for PAs in public practice); others: DE

³⁴ Regulator: IRBA; member bodies: ACCA, AICPA, CICA, CIMA, CIPFA, CPAA, FAR, HKICPA, ICAA, ICAEW, ICAP, ICAS, ICJCE, ICPAC, IDW, JICPA, KICPA, MIA, SAICA; firms: BDO, GT, DTT, EYG, KPMG, Kreston, Mazars, MG, PKF, PwC, RSM; other organizations: AAA (for PAIBs), APESB, CalCPA-APASC, CARB, EFAA, FEE, IIA, IMA, NASBA, SMPC

³⁵ Regulator: FAOA; member bodies: AICPA, CICA, CPAA, ICAP; firms: BDO, MG, RSM; other organizations: AAA (for PAIBs), APESB

³⁶ Member bodies: ACCA, HKICPA, ICAEW, ICJCE; Firms: DTT, Kreston, PKF, PwC; other organizations: FEE, IIA, NZAASB

³⁷ Member bodies: ACCA, MIA; firm: PKF

³⁸ Member bodies: ACCA, ICAEW, IDW; firm: Kreston

- It may not be possible for the auditor to feed back to the PA the action taken, or the auditor would be required to breach confidentiality by discussing the response with the PA.⁴⁰
33. A respondent from the regulatory community⁴¹ expressed support for the proposal that auditors be alerted to actual or suspected illegal acts that may be material to the financial statements. The respondent, however, did not support the proposal for the external auditor to be established as the default party to which a PA should disclose any concerns in circumstances where the PA is unable to escalate the matter within the entity or has doubts about the integrity or honesty of management and there is no established mechanism for reporting such matters (such as an ethics hotline). The respondent felt that while doubts about the integrity of management may be relevant to the auditor's role, the proposed requirement would also risk the auditor having to deal with vexatious reports or matters that are not relevant to the audit and are outside the auditor's expertise. The respondent also felt that having to deal with reports that are not relevant to the audit may detract the auditor's focus from matters that are relevant. The respondent did not believe it would be appropriate to extend the auditor's role and responsibilities in such a way, through an ethical code, rather than through law or regulation.
34. The same regulatory respondent also questioned why a PAIB would be required to disclose the SIA to the external auditor but not directly to an appropriate authority. The respondent felt that the proposed requirement could have adverse consequences such as an unacceptable delay in the authority being informed given that the auditor would need to undertake the auditor's own investigations before reporting to the authority. The respondent was of the view that if an appropriate authority exists, the PA should be required to disclose concerns directly to that authority rather than use the auditor as a conduit. The respondent noted that in such a case it would be helpful if the auditor were informed (subject to any legal, regulatory or contractual confidentiality requirements) of any such reports or other concerns considered relevant to the audit of the financial statements.

Respondents' Alternative Suggestions

35. Several of the respondents suggested that rather than being a requirement, disclosure to an external auditor should be an option, as a requirement would be counter-productive.⁴²
36. A few⁴³ suggested that if the matter were related to an audit, it would be appropriate to encourage the PA to inform the auditor.
37. A few others suggested, for a PAIB, communicating with the internal audit function (if applicable) instead.⁴⁴

³⁹ Member body: ICAEW, ICAS, ICJCE, MIA; other organization: FEE

⁴⁰ Member body: ICAEW; firm: Mazars

⁴¹ FRC

⁴² Member bodies: ICAA, ICPAC, ICAEW, MIA, SAICA; firm: EYG; other organizations: APESB, EFAA, IIA, SMPC

⁴³ ICAEW, SMPC

⁴⁴ Member bodies: CIPFA, NBA

Matter for Consideration

IESBA members are asked for views on, and reactions to, respondents' comments and suggestions above.

C. RIGHT WITH EXPECTATION TO DISCLOSE TO AN APPROPRIATE AUTHORITY

38. The ED proposed that a PA providing non-audit services to a non-audit client and a PAIB would be required to disclose certain SIAs to the entity's external auditor, if any, and, in certain circumstances, would have a right to disclose the SIAs to an appropriate authority and would be expected to exercise that right. The explanatory memorandum asked respondents whether they agreed with the proposal in the context of both PAs providing services to non-audit clients and PAIBs.
39. Overall, the level of opposition to this proposal has been significant, although this is tempered somewhat by many of those against the proposal coming forward with their views as to what they would be prepared to support.
40. While a small minority of respondents were supportive of the proposal in both contexts,⁴⁵ a significant majority⁴⁶ was opposed to, or had significant concerns regarding, the proposal. The most significant objection⁴⁷ came on the grounds that the combination of the right and the expectation amounted to a de facto obligation on the PA. Other related concerns included the following:
- The proposal could not be supported as only law or regulation can grant such a right.⁴⁸
 - Some respondents⁴⁹ were of the view that a right is granted in law and therefore it is a jurisdictional matter. They argued that the IESBA does not have the authority to grant a unilateral right to breach statutory, regulatory or contractual obligations, including with respect to confidentiality. Instead, they felt that what is being considered is whether it would be appropriate for the PA to override confidentiality within the boundaries of the legal framework.

Respondents' Alternative Suggestions

41. Many respondents⁵⁰ who were opposed to the combination of a right and an expectation indicated that they would support a right but not with an expectation that the right would be exercised.

⁴⁵ Member bodies: CICPA, CNDCEC, ICPAC, ICPAK, ICPAR, ICPAU, ZICA; others DE

⁴⁶ Regulator: IRBA; member bodies: ACCA, AICPA, CGA, CIMA, CIPFA, CNDCEC, CPAA, FAR, HKICPA, ICAA, ICAEW, ICAP, ICAS, ICJCE, ICPAK, IDW, JICPA, KICPA, MIA, SAICA; firms: BDO, DTT, EYG, GT, KPMG, Kreston, MG, Mazars, PKF, PwC, RSM; other organizations: APESB, CalCPA-APASC, CARB, EFAA, FEE, IIA, IMA, NASBA, PAIBC, PICPA, SMPC

⁴⁷ Member bodies: AICPA, CGA, CNDCEC, CPAA, HKICPA, ICAEW, IDW, MIA; firms: DTT, EYG, GT, Mazars, PKF; other organizations: NASBA, PAIBC, PICPA, SMPC.

⁴⁸ Regulator: FAOA; member body: CICA; firm: PKF; other organizations: AAA, CalCPA-APASC, PAIBC

⁴⁹ Member bodies: ICAEW, IDW, JICPA; firm: PwC; other org: NASBA

⁵⁰ Member bodies: ACCA, CPAA, HKICPA, ICAA, ICAEW, ICAS, MIA, SAICA; firms: GT, PKF, RSM; other organizations: APESB, CARB, EFAA, IIA, IMA, SMPC

Matter for Consideration

IESBA members are asked for views on, and reactions to, respondents' comments and suggestions above.

III. Secondary Issues

42. The following section summarizes respondents' significant comments on a number of issues that, while not of a pivotal nature, nevertheless are critical to exploring a practicable way forward. The IESBA is asked to share views on, and reactions to, respondents' comments and suggestions outlined below.

D. THE PUBLIC INTEREST TEST AND THE ESCALATION THRESHOLD

The Public Interest Test

43. The explanatory memorandum to the ED asked for respondents' views as to whether they agreed with using the public interest as the reporting threshold. Views were mixed.
44. While many⁵¹ were generally supportive of the proposed threshold, a significant number of them⁵² expressed concern about the lack of a definition of the term in the ED or guidance that would facilitate consistent application.
45. A regulatory respondent suggested that the IESBA should "revisit the role of the 'public interest' filter, since it seems that it would be in the public interest for any suspected violation to be subjected to the appropriate handling."⁵³
46. Many other respondents did not support the proposed threshold, with several of them believing that it was a fundamental issue. Significant concerns expressed included the following:
- The public interest test is too broad and vague. The concept of public interest itself is undefined and little guidance has been provided on how it should be applied. Also, it is very subjective and too complex and abstract to be applied uniformly and appropriately to all services provided by PAs. Further, the test of a reasonable and informed third party is too judgmental, especially when taking into account cultural differences.⁵⁴
 - It should not be left to PAs to determine significance in a legal context as this may not be within their competence. Guidance on significance probably cannot be realistically provided on an international basis.⁵⁵

⁵¹ Member bodies: ACCA, ICAA, CICA, CICPA, CIMA, CIPFA, CNDCEC, CPAA, FAR, HKICPA, ICAA, ICAEW, ICAP, ICPAC, ICPAK, ICPAR, ICPAU, MIA, SAICA, ZICA; firms: GT, Mazars, RSM; other organizations: AAA, APESB, CARB, EFAA, IIA, IMA, PAIBC

⁵² Member bodies: ACCA, CICA, CICPA, CIMA, CPAA, FAR, HKICPA, ICAEW, ICAP, ICAS, SAICA; firms: Mazars, PKF; other organizations: AAA, APESB, CARB, EFAA

⁵³ IOSCO

⁵⁴ Regulator: IRBA; member bodies: AICPA, CAI, CNCC, FSR, ICJCE, ICPAC, IDW, JICPA, KICPA, MIA, WPK; firms: BDO, DTT, EYG, Kreston, MG, PwC, RSM; other organizations: Assirevi, CCAB, FEE, GLW, NASBA, NZAASB, SMPC

⁵⁵ Member bodies: ICJCE, MIA; firm: Mazars; other organization: FEE

- National authorities should establish reporting thresholds, or the proposed threshold should only apply where disclosure is required by law or regulation.⁵⁶
- Many PAs will not know how to make an assessment in the public interest, and therefore few matters would be reported in practice.⁵⁷

Escalation Threshold

47. Many respondents⁵⁸ expressed concern that the ED appeared to call for escalation and therefore eventual reporting of any SIA regardless of materiality or significance. It was noted in particular that for small- and medium-sized entities (SMEs), potentially a wide range of minor suspected illegal acts could be reported, internally and possibly externally, which would be disproportionate and unlikely to be in the public interest. It was also noted that small and medium practices (SMPs) may potentially be held to a higher standard than larger firms (which may find fewer SIAs on the grounds that audits of larger entities are undertaken to higher materiality levels).
48. It was also felt that the word “suspected” should be replaced with “likely” or a similar word on the grounds that, while the threshold of “suspected” may be appropriate when investigating and escalating the matter within the entity, for reporting purposes it is a low threshold.⁵⁹

Respondents’ Alternative Suggestions

49. Some of the respondents⁶⁰ suggested that materiality to the financial statements may be a more concrete threshold for considering reporting.
50. A suggestion that was also made was for consideration to be given to developing a reporting threshold modeled on exceptions to confidentiality that exist for other professionals. For example, for psychiatrists, disclosures of otherwise confidential information are sometimes statutorily permitted to avoid serious or imminent harm to third parties.⁶¹
51. It was also suggested that if the public interest test were to be retained, the IESBA should leverage IFAC’s Policy Position 5 on a definition of public interest, or work with IFAC in developing appropriate guidance on the meaning of the public interest.⁶²

Matter for Consideration

IESBA members are asked to share views on, and reactions to, respondents’ significant comments described above. In particular, IESBA members are asked whether the public interest test should be retained, even if there no longer were to be a requirement for PAs to disclose certain SIAs to an appropriate authority and, instead, permission granted in the Code for an override of confidentiality in

⁵⁶ Regulators: FAOA; member bodies: ICAS, IDW, JICPA; firms: KPMG, PKF

⁵⁷ Member body: IDW; firms: Kreston, Mazars

⁵⁸ Member bodies: ACCA, AICPA, FSR, ICJCE, IDW, SAICA; firms: BDO, DTT, EYG, Mazars, MNP, PKF, PwC; other organizations: EFAA, FEE, IMA, NASBA, SRA, USCC

⁵⁹ EYG

⁶⁰ Regulator: IRBA; firms: BDO, MG, RSM

⁶¹ EYG

⁶² Firms: PKF, PwC

certain circumstances.

E. REQUIREMENT TO CONFIRM OR DISPEL THE SUSPICION

52. The ED proposed to require a PA when encountering a SIA to take reasonable steps to confirm or dispel the suspicion and to discuss the matter with the appropriate level of management. The explanatory memorandum also asked respondents whether they agreed with the proposed escalation process. Respondents' views were about equally divided on this issue.
53. Many of the respondents⁶³ were supportive of the proposal, including the related escalation process, although some recognized the potential for a number of significant practical challenges in applying the requirement. In this regard, a respondent from the regulatory community⁶⁴ was of the view that the proposed provisions on the process before the PA arrives at a determination to report should be clarified and made more specific, including the related expectations and responsibilities, to ensure enforceability.
54. Many other respondents,⁶⁵ however, were opposed to the proposal because of what they perceived to be a number of fundamental practical constraints arising from the prescriptive nature of the requirement. Concerns expressed included the following:
- The PA may not have the relevant expertise or experience to establish whether a matter is illegal. Given the fundamental principle of professional competence, the Code effectively prevents a PA from making legal interpretations without appropriate competence. In addition, it was questioned whether a suspicion could be dispelled without the expertise of a lawyer.
 - It was unclear what the appropriate evidence would be to confirm or dispel a suspicion.
 - The PA may be unable to make a reasonable assessment of the matter because of practical limitations in obtaining access to relevant information (e.g., data sources may be protected by legal privilege), potentially leading to an increase in erroneous disclosures.
 - The investigation may lead to tipping-off and, therefore, potentially inadvertently cause a breach of laws such as anti-money laundering legislation that prohibit tipping-off.
 - The requirement may call for a significant amount of work and therefore cost to establish likelihood of a SIA. It was unclear who would pay for this work. In addition, such a requirement could lead to high risks to personal safety.
 - It is effectively left to the PA's judgment to determine whether remedial action is sufficient.
 - The engagement may have ended by the time management completes its evaluation.
55. A number of the respondents also objected to the proposed requirement on the grounds that it would turn PAs into investigators and prosecutors. It was argued that investigations should be the

⁶³ Regulator: FAOA; member bodies: CICPA, CIMA, CNDCEC, FAR, ICAEW, ICAP, ICPAC, ICPAK, ICPAR, ICPAU, CICA, JICPA, KICPA, MIA, SAICA, ZICA; firms: BDO, GT, KPMG, Mazars, MG, RSM; other organizations: AAA, APESB, CalCPA-APASC, CGA, EFAA, IMA, NASBA

⁶⁴ 7AR

⁶⁵ Regulator: IRBA; member bodies: ACCA, AICPA, CPAA, CIPFA, HKICPA, ICAEW, ICAA, ICAP, ICAS, IDW, KICPA, MIA; firms: BDO, DTT, EYG, GT, Kreston, MG, MNP, PKF, PwC, RSM; other organizations: CalCPA-CPC, CARB, EFAA, FEE, GLW, IIA, IMA, NASBA, PAIBC, PICPA, SMPC, SRA, USCC

responsibility of enforcement authorities.⁶⁶ It was also argued that the proposal would unreasonably broaden auditors' responsibilities far beyond auditing standards by requiring them to investigate SIAs of which they have become aware through performance of the audit, disclosure by a PA employed by their audit client; or information communicated by anyone in a PA firm performing non-assurance services for the client.

56. Some respondents pointed out that the ED did not appear to have addressed the possibility that the PA may be unable to confirm or dispel the suspicion.⁶⁷
57. Many respondents also questioned the lack of guidance regarding the meaning of:
- "Reasonable steps" in confirming or dispelling a suspicion.⁶⁸
 - A suspicion.⁶⁹ It was noted that the point at which the PA would be required to take reasonable steps to confirm or dispel the suspicion was undefined. It was also felt that a suspicion of an illegal act is a relatively low test.⁷⁰ There were some suggestions that the bar be set at "likely" or "more likely than not."⁷¹

Respondents' Alternative Suggestions

58. Some respondents expressed support for different options as follows:
- The PA should be permitted to exercise judgment as to the best course of action.⁷²
 - The correct route should be to follow established procedure within the entity, including tapping into any whistle-blower mechanisms that may already be in place, report to internal auditors, or obtain legal advice.⁷³
 - The auditor should comply with the requirements of ISA 250⁷⁴ in these circumstances.⁷⁵

Matters for Consideration

The Task Force believes that this aspect of the ED will remain one of continuing debate as the IESBA explores a way forward. Given the significant practical concerns expressed by respondents above, it appears that the requirement to confirm or dispel the suspicion could place a more onerous burden of proof on the PA than what might have been originally envisaged.

The Task Force notes that the requirements in ISA 250 relative to the auditor's procedures when the auditor has identified an actual or suspected case of non-compliance with laws or regulations appear to

⁶⁶ Member bodies: ICAP, IDW, WPK; firms: Kreston, MG, PKF, PwC, RSM

⁶⁷ Member bodies: ICAEW, NBA; other organizations: EFAA, SMPC

⁶⁸ Member bodies: ACCA, AICPA, CIMA, ICJCE, JICPA.; firms: DTT, KPMG, Kreston, PwC, RSM; other organizations: SMPC, USCC

⁶⁹ Member bodies: AICPA, CGA, CIMA, CPAA, IBR, JICPA; firms: DTT, KPMG, PwC; other organizations: AAA, FEE, SMPC

⁷⁰ Member body: AICPA; other organizations: EFAA, NZAASB

⁷¹ Member bodies: AICPA, IDW; other organization: NASBA

⁷² Member bodies: CPAA, ICAA; firm: PKF

⁷³ Member bodies: CIMA, JICPA, NBA; firm: Kreston; other organizations: IIA, PAIBC

⁷⁴ ISA 250, *Consideration of Laws and Regulations in an Audit of Financial Statements*

⁷⁵ Member bodies: ACCA, ICJCE; firm DTT; other organization: FEE

be generally less prescriptive (see paragraphs 18-21 of ISA 250 in Agenda Item 2-C).

The IESBA is asked for its views on, and reactions to, respondents' comments and suggestions above. In particular:

- (a) Would there be merit in considering approaching the PA's response in a less prescriptive manner, such as by providing guidance regarding matters the PA may consider in determining the most appropriate response?
- (b) Would it be more appropriate to adopt a "reason to believe" test (which is already used in various places in the Code) or some other threshold as the trigger for a response from the PA, as opposed to a "suspicion" of an illegal act?

F. MEANING OF KEY TERMS

Appropriate Authority

- 59. With regard to the proposed requirement or right to disclose a SIA to an appropriate authority, many respondents⁷⁶ noted uncertainty as to who the appropriate authority might be as the term was undefined. It was noted in particular that there could be a wide range of authorities at different levels of government (for example, federal, state and city) in a given jurisdiction.
- 60. A few respondents commented that the ED did not appear to have taken into account the capacity and effectiveness of the legal system to respond to the disclosures.⁷⁷
- 61. Some respondents also noted that not all countries may have an appropriate authority, particularly if reporting is not mandated in law.⁷⁸

Suspected Illegal Act

- 62. Many respondents⁷⁹ also questioned the lack of guidance regarding the meaning of a SIA. In particular, it was noted that the concept of a SIA appears very broad and that what is a SIA may differ amongst jurisdictions. It was also noted that defining the term may be very difficult but that without clarity, there would be uncertainty and possibly unenforceability.
- 63. A regulatory respondent commented that the Code should specifically mention that SIAs encompass suspected frauds. The respondent also suggested that the IESBA establish whether this project will encompass acts of personal misconduct that are associated with employment (e.g., employees or their close family members selling company shares at inappropriate times).⁸⁰

⁷⁶ Member bodies: ACCA, AICPA; firms: BDO, EYG, KPMG, MG, RSM; other organizations: AAA, APESB, Assirevi, FEE

⁷⁷ Regulator: IOSCO; member bodies: FAR, IDW; firm: DTT

⁷⁸ Member bodies: ICJCE, IDW, JICPA; firms: KPMG, Kreston; other organization: FEE

⁷⁹ Member bodies: CICA, CGA, CPAA, FSR, HKICPA, IBR, ICAP, ICJCE, KICPA, SAICA; firms: DTT, KPMG; other organizations: AAA, EFAA, NZAASB, SMPC

⁸⁰ IOSCO

Matters for Consideration

IESBA members are asked to share reactions to respondents' concerns above. IESBA members are also asked for views as to whether the Task Force should explore further guidance on the concepts of an appropriate authority and a SIA.

G. TYPES OF SIAs TO BE DISCLOSED

64. The ED asked respondents whether they agreed with the proposed types of SIAs to be disclosed by PAs categorized in three groups, i.e.:

- For a PA in public practice providing services to an audit client:
 - SIAs that directly or indirectly affect the client's financial reporting; and
 - SIAs the subject matter of which falls within the PA's expertise.
- For a PA in public practice providing services to a non-audit client:
 - SIAs that relate to the subject matter of the professional services being provided by the PA. (This recognized the limited scope of the engagements in these circumstances.)
- For a PAIB:
 - SIAs that directly or indirectly affect the employing organization's financial reporting; and
 - SIAs the subject matter of which falls within the PA's expertise.

PAs in Public Practice Providing Services to an Audit Client

65. Many of the respondents⁸¹ who addressed the question were supportive of the proposed types of SIAs to be disclosed for PAs providing services to an audit client.
66. A majority,⁸² however, disagreed. Several⁸³ felt that any restriction is inconsistent with the public interest argument used to justify a requirement or right to disclose, or would be inappropriate in a code dealing with "ethics." Many others⁸⁴ recorded their disagreement on the grounds that they did not support a disclosure requirement for these PAs except if it were in law or regulation. A few⁸⁵ were of the view that the types of SIAs to be disclosed should be determined by national authorities. A few others⁸⁶ favored limiting the types of SIAs to be disclosed to only matters that materially affect financial reporting.

⁸¹ Member bodies: CNDCEC, HKICPA, ICAEW, ICPAK, ICPAR, ICPAU, KICPA, MIA, ZICA; firms: EYG, KPMG; other organizations: AAA, APESB, CARB, IIA, NASBA

⁸² Regulators: FAOA, IRBA; member bodies: ACCA, AICPA, CICA, CICPA, CGA, CPAA, FAR, ICAA, ICAP, ICAS, ICJCE, ICPAC, IDW, JICPA, SAICA; firms: BDO, DTT, GT, Kreston, Mazars, MG, MNP, PKF, PwC, RSM; other organizations: CalCPA-APASC, CCAB, EFAA, FEE, SMPC

⁸³ Member bodies: ACCA, CICA, ICAS, ICJCE; firms: Mazars, PKF; other organizations: CalCPA-APASC, EFAA, FEE

⁸⁴ Regulators: FAOA, IRBA; member bodies: AICPA, CPAA, FAR, ICAA, ICJCE, SAICA; firms: BDO, DTT, GT, MG, RSM; other organizations: SMPC

⁸⁵ Member body: JICPA; firm: Kreston

⁸⁶ Member bodies: CGA, ICAP

PAs in Public Practice Providing Services to a Non-Audit Client

67. While many of the respondents⁸⁷ who commented on this question were supportive of the proposed types of SIAs to be disclosed for PAs providing services to a non-audit client, a greater number⁸⁸ disagreed.
68. Several of the respondents⁸⁹ expressed their disagreement simply because they did not support a disclosure requirement in the Code for these PAs or because they felt that the disclosure should be the responsibility of management or TCWG. Several others⁹⁰ felt that there should be no limitation in scope, especially if a public interest rationale was used to justify disclosure.

PAIBs

69. Many of the respondents⁹¹ who commented on this question were supportive of the proposed types of SIAs to be disclosed for PAIBs.
70. A greater number,⁹² however, disagreed. Many⁹³ did not support the proposal simply because they were opposed to the Code imposing a disclosure obligation on PAIBs. Several of the respondents⁹⁴ felt that there should be no limitation in scope if the public interest was used to justify disclosure. A few of the respondents⁹⁵ flagged that it was unclear whether both conditions were intended to be met or whether they were mutually exclusive.

Matter for Consideration

Subject to the IESBA's consideration of the pivotal and secondary issues identified above and taking into account the Board's prior deliberations regarding the types of SIAs to be disclosed for the three different categories of PAs, IESBA members are asked to share any reactions to the significant respondent comments outlined above.

⁸⁷ Member bodies: CGA, CNDCEC, HKICPA, ICAEW, ICAP, ICPAK, ICPAR, ICPAU, JICPA, KICPA, SAICA, ZICA; firm: GT; other organizations: AAA, APESB, CARB, SMPC; other: DE

⁸⁸ Regulators: FAOA, IRBA; member bodies: ACCA, AICPA, CICA, CICPA, CPAA, FAR, ICAA, ICAS, ICJCE, ICPAC, IDW, MIA; firms: BDO, DTT, EYG, Kreston, Mazars, MG, KPMG, PKF, PwC, RSM; other organizations: CalCPA-APASC, EFAA, FEE, IIA, NASBA

⁸⁹ Regulator: IRBA; member bodies: AICPA, CPAA, FAR, ICAA, ICJCE; firms: BDO, MG, KPMG, RSM

⁹⁰ Regulator: FAOA; member bodies: CICA, ICAS; firms: DTT, Kreston, Mazars, PKF; other organization: CalCPA-APASC, EFAA, IIA, NASBA

⁹¹ Member bodies: CGA, CIMA, CIPFA, CNDCEC, HKICPA, ICAEW, ICPAK, ICPAR, ICPAU, KICPA, MIA, SAICA, ZICA; firm: GT; other organizations: AAA, APESB, CARB, NASBA, PAIB, SMPC; other: DE

⁹² Regulators: FAOA, IRBA; member bodies: ACCA, AICPA, CICA, CICPA, CPAA, FAR, ICAA, ICAS, ICJCE, ICPAC, IDW, MIA; firms: BDO, DTT, EYG, Kreston, Mazars, MG, KPMG, PKF, PwC, RSM; other organizations: CalCPA-APASC, EFAA, FEE, IIA, NASBA

⁹³ Regulator: FAOA; member bodies: AICPA, CPAA, FAR, ICAA, ICAP, ICJCE, IDW; firms: BDO, DTT, KPMG, RSM

⁹⁴ Member bodies: ACCA, CICA, ICAS; firm: PKF; other organizations: CalCPA-APASC, EFAA, IIA

⁹⁵ Member bodies: CIPFA, MIA

H. INTERACTION OF THE PROPOSED STANDARD WITH ISAs

71. Some respondents⁹⁶ noted that the ED is inconsistent with, or goes beyond, ISA 250. In particular, it was noted that the scope of the ED extends beyond SIAs affecting financial reporting to those falling within the PA's expertise. It was argued that this would require a change in approach under ISA 250. It was also noted that it was unclear how the proposals interact with ISAs 240⁹⁷ and 250.
72. As noted under Issues B and F above, significant concerns were also expressed regarding the potential for the proposals to expand the auditor's role and responsibilities beyond the ISAs.

Suggestions from Regulatory Respondents and Others

73. A few respondents from the regulatory community made the following comments and suggestions in relation to the interaction between the ED and the ISAs:
- There are a number of areas where considerations under ISA 250 overlap with those set out in the ED, in relation to action to be taken on becoming aware of a SIA and discussion of the matter with the appropriate level of management and TCWG. It would be unhelpful if requirements addressing the same issues were in two separate sets of standards that may both be applicable to auditors and that, whilst not apparently contradictory, are also not fully consistent.⁹⁸
 - The relationship between the proposed new sections in the Code and IAASB standards such as ISAs 240, 250, 580⁹⁹ and 700¹⁰⁰ could be explained. For example, it would be relevant to clarify whether and how SIAs also cover instances of fraud as defined in ISA 240.¹⁰¹
 - The proposals should be re-deliberated, taking into account responses to the ED. In doing so, the IESBA should establish the SIAs for which the auditor is called to take steps that are incremental to what is called for by the ISAs. In addition, the IESBA should establish what incremental steps the auditor is called to take beyond those called for by the ISAs¹⁰² (see further details in Issue A above).
 - Depending on the timing of the IAASB's current auditor reporting project, the IESBA could coordinate with the IAASB's conclusions from this project and/or establish incremental steps suggested in the respondent's comment letter relative to the existing ISA requirements for auditor reporting.¹⁰³
74. These regulatory as well as other respondents encouraged the IESBA to work with the IAASB in taking forward this project to ensure co-ordination in the finalization of the ethical requirements with the ISAs.

⁹⁶ Regulator: IRBA; member bodies: FAR, IDW; firm: MNP; other organization: Assirevi

⁹⁷ ISA 240, *The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements*

⁹⁸ FRC

⁹⁹ ISA 580, *Written Representations*

¹⁰⁰ ISA 700, *Forming an Opinion and Reporting on Financial Statements*

¹⁰¹ 7AR

¹⁰² IOSCO

¹⁰³ IOSCO

75. Other respondents¹⁰⁴ suggested that the ED should not go beyond what is required under the ISAs and that auditors should comply with ISA 250 and any national requirements.¹⁰⁵

Matters for Consideration

The Task Force notes that in developing the ED, the IESBA had not intended to introduce inconsistencies between the proposals and the ISAs. However, given the significant concerns expressed by respondents above and the regulatory comments that seem to suggest that there would be benefit in exploring enhancements to the ISAs (see IOSCO suggestions under Issue A above), the Task Force believes that liaison and coordination with the IAASB will be essential as this project moves forward.

The IESBA is asked:

- (a) For its views on, and reactions to, respondents' comments and suggestions above; and
- (b) Whether it agrees that formal liaison with the IAASB should be established in connection with this project, such as through the correspondent Task Force member mechanism.

IV. Other Issues

76. The Task Force has also summarized respondents' comments on the following significant aspects of the ED but has yet not formed a view as to how these should be addressed pending the IESBA's consideration of the pivotal issues, the outcome of which will largely influence how these other issues should be tackled. Nevertheless, the Task Force welcomes the IESBA's reactions to the significant ED comments outlined below and any directional input the Board may provide.

I. THE EXCEPTION PROVISION

77. The ED asked respondents whether they agreed that in exceptional circumstances a professional accountant should not be required, or expected to exercise the right, to disclose certain illegal acts to an appropriate authority and, if not, what action they believed should be taken. Among respondents who addressed this question, the balance overall was tilted towards those¹⁰⁶ supportive of the principle of allowing for exceptions, even though a number of them had fundamental concerns about the reporting requirement and the right with the expectation to report.
78. A significant minority of respondents¹⁰⁷ explicitly disagreed with the proposed provision simply because they did not support the external reporting requirement or the right with the expectation to report. It was noted, in particular, that if there were no requirement but only a right, there would be no need for exceptions. A few others felt that the provision should be subject to applicable law or regulation, or legal advice.¹⁰⁸

¹⁰⁴ Regulator: IRBA; member bodies: IDW, KICPA; firm: DTT

¹⁰⁵ Member bodies: ACCA, KICPA; firms: DTT, KPMG, Kreston

¹⁰⁶ Regulator: IRBA; member bodies: AICPA, CGA, CICA, CICPA, CNDCEC, FAR, HKICPA, ICAA, ICAP, ICAS, ICPAK, ICPAR, ICPAU, KICPA, SAICA, ZICA; firms: Kreston, Mazars, PKF, PwC; other organizations: AAA, APESB, EFPA, IIA, IMA, PAIBC, SMPC; other: DE

¹⁰⁷ Member bodies: CPAA, ICAEW, ICJCE, ICPAC, IDW, JICPA; firms: BDO, GT, MG, RSM; other organizations: CalCPA-APASC, CARB, NASBA

¹⁰⁸ Regulator: FAOA; member bodies: CIMA, ICAP

79. The ED also asked whether respondents agreed as to the appropriateness of the exceptional circumstances described in the proposal.¹⁰⁹ Among those supportive of allowing for exceptions, many¹¹⁰ agreed with, or did not object to, the description in the ED.
80. However, many others, including those who did not support the exception principle, felt that the circumstances described lacked clarity or were too limited.¹¹¹ Several suggested that additional guidance be provided or that the circumstances be broadened to include other considerations such as: no or inadequate legal protection; liability risks; and threats to personal property. Further, some were of the view that ruling out commercial considerations would have a disproportionate effect on PAIBs.¹¹²

Matter for Consideration

Subject to the IESBA's consideration of the pivotal and secondary issues identified above, the IESBA is asked to share any reactions to the significant ED comments described above.

J. SCOPE OF APPLICATION OF THE PROPOSED STANDARD

Applicability to PAs in Public Practice Providing Services to an Audit Client vs. a Non-Audit Client

81. The ED asked respondents whether they agreed that the standard for a professional accountant in public practice providing services to an audit client should differ from the standard for a professional accountant in public practice providing services to a client that is not an audit client.
82. Many respondents expressed support for a differential standard.¹¹³ A few of the respondents¹¹⁴ explicitly agreed with the IESBA's rationale that it would be appropriate to establish the more stringent standard for auditors because of their public interest role, and that PAs providing services to non-audit clients may not have appropriate access to management or those charged with governance.
83. A greater number,¹¹⁵ however, were opposed to any distinction being made, with most of them arguing that the type of service should not have any bearing on the PA's response if the benchmark used is the public interest. Some¹¹⁶ were of the view that any differentiation should be established in law or regulation.

¹⁰⁹ The ED stated the following: "Exceptional circumstances would arise where a reasonable and informed third party would conclude that the consequences of disclosure are so severe as to justify not complying with the requirement to disclose, for example, where there would be threats to the physical safety of the professional accountant or other individuals."

¹¹⁰ Member bodies: CICA, ICAS, ICPAR, ICPAU, KICPA, SAICA, ZICA; firms: Kreston, Mazars; other organizations: EFAA, IMA; other: DE

¹¹¹ Regulator: IRBA; member bodies: AICPA, CGA, CICPA, CNDCEC, CPAA, HKICPA, ICAA, ICPAK; firms: DTT, PwC; other organizations: AAA, APESB, CalCPA-APASC, IIA, PAIBC, SMPC

¹¹² Member bodies: CNDCEC, ICAP; other organizations: AAA, CCAB, PAIBC

¹¹³ Member bodies: ACCA, AICPA, CICPA, CNDCEC, FAR, HKICPA, ICAP, ICPAR, JICPA, SAICA, ZICA; firms: GT, MG, RSM; other organizations: AAA, IIA

¹¹⁴ Member bodies: ACCA, JICPA, SAICA

¹¹⁵ Regulators: FAOA, IRBA; member bodies: CGA, CICA, CIPFA, CPAA, ICAA, ICAEW, ICAS, ICJCE, ICPAC, ICPAK, ICPAU, IDW, MIA; firms: BDO, DTT, GT, KPMG, Kreston, Mazars, PKF, PwC; other organizations: AAA, APESB, CalCPC-APASC, CCAB, CARB, EFAA, FEE, NASBA, SMPC

¹¹⁶ Regulator: FAOA; firms: DTT, Kreston; other organization: FEE

Applicability to PAs Providing Professional Services to an Audit Client vs. Auditors

84. The ED asked respondents whether they agreed that a PA providing professional services to an audit client of the firm or a network firm should have the same obligation as an auditor. The majority of respondents¹¹⁷ who addressed this question were in agreement that no distinction should be made.
85. A significant minority disagreed,¹¹⁸ with some¹¹⁹ noting that they could only support the proposal if there were only a right and not a requirement to report, or when the PA is not acting in a fiduciary capacity. A few¹²⁰ were of the view that there should not be the same obligation as PAs providing non-assurance services to the audit client do not have the same access to information as auditors. A few others¹²¹ felt that any differentiation should be established in law or regulation.
86. Some of the respondents¹²² suggested that if the SIA relates to the financial statements, it may be appropriate for the PA providing the non-assurance service to alert the audit engagement partner and for the latter to appropriately escalate the matter.

Matter for Consideration

Subject to the IESBA's consideration of the pivotal and secondary issues identified above and taking into account the Board's prior deliberations regarding the scope of application of the proposed standard, IESBA members are asked to share any reactions to the significant respondent comments described above.

K. DOCUMENTATION

87. The ED asked respondents whether they agreed with the documentation requirements in the proposed Sections 225 and 360. Views on this question were divided. Many respondents were supportive of the requirements as proposed,¹²³ with a few¹²⁴ suggesting that further guidance be provided to facilitate proportionate application and to avoid PAs inadvertently prejudicing the legal process.
88. Many others, however, were opposed to the proposal.¹²⁵ In particular, several of them were concerned that:¹²⁶

¹¹⁷ Regulators: FAOA, IRBA; member bodies: ACCA, AICPA, CGA, CIPFA, CNDCEC, FAR, ICAEW, ICAP, ICJCE, ICPAC, ICPAK, ICPAR, ICPAU, KICPA, MIA, ZICA; firms: BDO, KPMG, Mazars, PKF, RSM; other organizations: AAA, CalCPA-APASC, CARB, CCAB, EFAA, IIA, NASBA, SMPC

¹¹⁸ Member bodies: CICA, CICPA, CPAA, HKICPA, ICAA, ICAS, IDW, JICPA, SAICA; firms: DTT, GT, Kreston, MG, PwC; other organizations: APESB, FEE; others: DE

¹¹⁹ Member bodies: CICA, ICAA, ICAS; firms: DTT, GT, MG; other organization: APESB

¹²⁰ Member bodies: CICPA, HKICPA

¹²¹ Member body: CPAA; firm: Kreston

¹²² Member bodies: AICPA, JICPA; firms: MG, RSM; other organizations: APESB, SMPC

¹²³ Regulator: FAOA; member bodies: CGA, CICA, CICPA, FAR, ICAP, ICAS, ICPAC, ICPAK, ICPAR, ICPAU, JICPA, KICPA, MIA, SAICA, ZICA; firms: Kreston; other organizations: AAA, APESB, CalCPA-APASC, CARB, EFAA, IIA, NASBA, PAIBC

¹²⁴ Member body: SAICA; other organization: APESB

¹²⁵ Regulator: IRBA; member bodies: ACCA, AICPA, CIMA, CNDCEC, CPAA, HKICPA, ICAA, ICAEW, ICAS, ICJCE, IDW; firms: BDO, DTT, EYG, GT, KPMG, Mazars, MG, PKF, PwC, RSM; other organizations: FEE, SMPC

- The requirements would be disproportionate as they seemed to call for documentation regardless of whether the SIAs were of any consequence; and
 - The resulting documentation may be legally discoverable.
89. Several others were of the view that the proposal seemed to move the Code away from its current position of generally advocating documentation in the PA's interests but not requiring it.¹²⁷ A few others felt that the ED went too far in proposing a documentation requirement for PAIBs and that any such requirement should be limited to PAs performing audit engagements.¹²⁸ Even then, however, a view was expressed that documentation requirements are adequately addressed elsewhere in professional standards.
90. The Task Force notes that in putting forth the proposed requirements, the IESBA had concluded that it would not be appropriate to make the documentation subject to a materiality threshold. The IESBA had in particular noted that ISA 260¹²⁹ requires documentation of identified or suspected non-compliance with laws and regulations without regard to materiality.
91. The IESBA had also noted that while PAIBs may encounter a larger number of immaterial SIAs in practice, the proposal would not require extensive documentation of every individual SIA. To explain the IESBA's thinking in this regard, the explanatory memorandum to the ED provided the example of an organization in the retail industry that is susceptible to regular but minor acts of pilferage. The explanatory memorandum indicated that in these circumstances the documentation requirements would be met by having a policy or procedure to address such matters. The IESBA had therefore already intended the level of documentation to be commensurate with the gravity of the SIA.

Matter for Consideration

Subject to the IESBA's consideration of the pivotal and secondary issues identified above and taking into account the Board's prior deliberations on this aspect of the ED, IESBA members are asked to share any reactions to the significant respondent comments described above.

¹²⁶ Regulator: IRBA; member bodies: CPAA, HKICPA, ICAA, ICAEW; firms: BDO, PKF, PwC; other organizations: FEE, SMPC

¹²⁷ Member bodies: ACCA, AICPA, CIMA, HKICPA, ICAA, ICAEW, ICAS; firms: DTT, MG, RSM

¹²⁸ Member body: CNDCEC; firm: KPMG

¹²⁹ ISA 260, *Consideration of Laws and Regulations on an Audit of Financial Statements*

Appendix 1

List of Respondents to the ED

Respondents		Overall Support?		
Abbr.	Organization	Yes	Part Support / Concern	No
IFAC MEMBER BODIES				
ACCA	Association of Chartered Certified Accountants (UK)			✓
AICPA	American Institute of Certified Public Accountants			✓
CAI	Chartered Accountants Ireland			✓
CGA	Certified General Accountants Canada			✓
CICA	The Canadian Institute of Chartered Accountants			✓
CICPA	Chinese Institute of Certified Public Accountants	✓		
CIMA	Chartered Institute of Management Accountants (UK)		✓	
CIPFA	Chartered Institute of Public Finance & Accountancy (UK)		✓	
CNCC	Compagnie Nationale des Commissaires aux Comptes and Conseil Supérieur de l'Ordre des Experts-Comptables (France)			✓
CNDCEC	Consiglio Nazionale dei Dottori Commercialisti E Degli Esperti Contabili (Italy)	✓		
CPAA	CPA Australia			✓
FAR	FAR (Sweden)			✓
FSR	Foreningen af Statsautoriserede Revisorer (Denmark)			✓
HKICPA	Hong Kong Institute of Certified Public Accountants			✓
IBR-IRE	Institut des Reviseurs d'Entreprises / Instituut der Bedrijfsrevisoren (Belgium)			✓
ICAA	The Institute of Chartered Accountants in Australia			✓
ICAEW	The Institute of Chartered Accountants in England and Wales			✓
ICAI	The Institute of Chartered Accountants of India		✓	
ICAP	The Institute of Chartered Accountants of Pakistan			✓

Respondents		Overall Support?		
Abbr.	Organization	Yes	Part Support / Concern	No
ICAS	The Institute of Chartered Accountants of Scotland			✓
ICJCE	Instituto de Censores Jurados de Cuentas de España			✓
ICPAC	Institute of Certified Public Accountants of Cyprus	✓		
ICPAK	Institute of Certified Public Accountants of Kenya	✓		
ICPAR	Institute of Certified Public Accountants of Rwanda	✓		
ICPAU	Institute of Certified Public Accountants of Uganda	✓		
IDW	Institut der Wirtschaftsprüfer (Germany)			✓
JICPA	The Japanese Institute of Certified Public Accountants			✓
KICPA	Korean Institute of Certified Public Accountants			✓
MIA	Malta Institute of Accountants			✓
NBA	Nederlandse Beroepsorganisatie van Accountants			✓
SAICA	The South African Institute of Chartered Accountants			✓
WPK	Wirtschaftsprüferkammer (Germany)			✓
ZICA	Zambia Institute of Chartered Accountants	✓		
FIRMS				
BDO	BDO International Ltd			✓
DTT	Deloitte Touche Tohmatsu			✓
EYG	Ernst & Young Global Ltd			✓
GT	Grant Thornton International Ltd			✓
KPMG	KPMG IFRG Ltd			✓
Kreston	Kreston International			✓
Mazars	Mazars			✓
MG	McGladrey LLP			✓
MNP	MNP LLP			✓
PKF	PKF International Limited			✓
RSM	RSM International			✓

Respondents		Overall Support?		
Abbr.	Organization	Yes	Part Support / Concern	No
PwC	PwC			✓
REGULATORS & PUBLIC AUTHORITIES				
7AR	Group of seven European Audit Regulators		✓	
FAOA	Swiss Federal Audit Oversight Authority	✓		
FRC	Financial Reporting Council (UK)		✓	
IOSCO	International Organization of Securities Commissions		✓	
IRBA	Independent Regulatory Board for Auditors (South Africa)			✓
NATIONAL STANDARD SETTERS				
APESB	Accounting Professional & Ethical Standards Board Limited (Australia)			✓
NZAuASB	New Zealand Auditing and Assurance Standards Board			✓
OTHER PROFESSIONAL ORGANIZATIONS				
AAA	American Accounting Association		✓	
APPC	Australian Public Policy Committee			✓
Assirevi	Associazione Italiana Revisori Contabili (Italy)			✓
CalCPA-APASC	California Society of CPAs – Accounting Principles and Auditing Standards Committee			✓
CalCPA-CPC	California Society of CPAs – Committee on Professional Conduct			✓
CARB	Chartered Accountants Regulatory Board (Ireland)			✓
CCA	Czech Chamber of Auditors			✓
CCAB	Consultative Committee of Accountancy Bodies (UK)			✓
EFAA	European Federation of Accountants and Auditors for SMEs		✓	
FEE	Fédération des Experts Comptables Européens			✓
IFA	Institute of Financial Accountants (UK)		✓	
IIA	The Institute of Internal Auditors		✓	

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Respondents		Overall Support?		
Abbr.	Organization	Yes	Part Support / Concern	No
IMA	Institute of Management Accountants (US)			✓
NASBA	National Association of State Boards of Accountancy (US)			✓
PAIBC	IFAC Professional Accountants in Business Committee			✓
PICPA	Pennsylvania Institute of Certified Public Accountants			✓
SMPC	IFAC Small and Medium Practices Committee			✓
SRA	SRA (Netherlands)			✓
USCC	U.S. Chamber of Commerce			✓
INDIVIDUALS & OTHERS				
DE	Denise Silva Ferreira Juvenal	✓		
GLW	GLW Analysis Services Pty Ltd			✓
TOTAL RESPONSES		9	10	54

Appendix 2

Exploring a Way Forward

1. The Task Force has explored on a preliminary basis possible ways to address respondents' significant concerns with respect to the pivotal issues and has identified the following as a possible approach for further consideration, subject to the IESBA's views and reactions.

Outline of a Possible Way Forward

FOR ALL PAs

*Enhancement to Section 110*¹³⁰

2. Paragraph 110.2 of the Code requires the following:

A professional accountant shall not knowingly be associated with reports, returns, communications or other information where the professional accountant believes that the information:

- (a) Contains a materially false or misleading statement;
- (b) Contains statements or information furnished recklessly; or
- (c) Omits or obscures information required to be included where such omission or obscurity would be misleading.

When a professional accountant becomes aware that the accountant has been associated with such information, the accountant shall take steps to be disassociated from that information.

3. The Task Force believes that what appears to be missing from Section 110 is an overarching provision that would address the PA's ethical obligation to not be associated with a client or an employer that is engaged in illegal or unethical acts. Setting aside for the time being the issues of scope and definition regarding the concepts of "illegal acts" and "unethical acts," the Task Force suggests that consideration be given to including such a provision in Section 110, which would then serve to guide and encourage PAs to do the right thing:

SECTION 110

Integrity

- Avoidance of association with an employer or client who engages in illegal or unethical acts.

*Introduction of a Permission in Section 140*¹³¹ *for PAs to Override Confidentiality in Certain Circumstances*

4. Section 140 establishes the overall principle and duty of confidentiality. It sets out the following circumstances where professional accountants are or may be required to disclose confidential information or when such disclosure may be appropriate, i.e.:
 - (a) Disclosure is permitted by law and is authorized by the client or the employer;
 - (b) Disclosure is required by law, for example:

¹³⁰ Section 110, *Integrity*

¹³¹ Section 140, *Confidentiality*

- (i) Production of documents or other provision of evidence in the course of legal proceedings; or
 - (ii) Disclosure to the appropriate public authorities of infringements of the law that come to light; and
- (c) There is a professional duty or right to disclose, when not prohibited by law:
- (i) To comply with the quality review of a member body or professional body;
 - (ii) To respond to an inquiry or investigation by a member body or regulatory body;
 - (iii) To protect the professional interests of a professional accountant in legal proceedings; or
 - (iv) To comply with technical standards and ethics requirements.
5. Given the high level of opposition to the proposed requirement for, and the right with the expectation of, disclosure to an appropriate authority, the Task Force believes that the IESBA should not pursue these proposals. The Task Force proposes that consideration be instead given to introducing in Section 140 the principle that the PA may be permitted to override confidentiality in certain circumstances if the PA believes that doing so would be in the public interest and disclosure would not be prohibited by law or regulation. The Task Force notes that some IFAC Member Bodies already have such a principle in their ethical codes.
6. Taking this approach would have the advantage of overcoming many of the practical difficulties respondents have highlighted with respect to operationalizing the two above proposals in the ED. Guidance could be provided to make clear that there would be no expectation that PAs would override confidentiality and disclose SIAs to an appropriate authority.
7. The key elements of Section 140 could then be as follows:

SECTION 140

Confidentiality

- General requirement to maintain confidentiality.
- PA may be required to override principle of confidentiality in certain circumstances.
- PA may be permitted to override principle of confidentiality in certain circumstances if the PA believes doing so is in the public interest.

8. Guidance could be provided on relevant factors to consider in determining whether disclosure would be appropriate in the public interest.

RESPONDING TO SIAs

9. The Task Force believes that a PA has an ethical responsibility to appropriately respond when encountering a SIA and not turn a blind eye to the act. Notwithstanding this, however, the Task Force acknowledges the significant level of opposition from respondents to what they may have perceived to be a rigid and prescriptive set of proposals in the ED. A contrasting sentiment from the responses seems, instead, to be that a more flexible approach, couched in terms of guidance regarding what a PA's options might be when facing a SIA, would have been more appropriate.

10. Accordingly, the Task Force suggests that the proposed Sections 225 and 360 in the ED be retained but taking the following alternative approaches.
11. First, the Task Force believes that the provision in the ED for PAs to comply with any applicable law and regulation that deals with responding to SIAs should be retained. So, for both Sections 225 and 360:
 - Consider whether there are any legal or regulatory requirements relating to the matter and, if so, the PA's first duty is to comply with those requirements.
12. The Task Force then felt that a less prescriptive approach should be taken to specifying the PA's response to a SIA, as follows.
13. Consideration should be given to using a "reason to believe" test as the threshold for initiating a response to a SIA. Such a test is already used in the Code and is a higher threshold than information that leads the PA to suspect an illegal act may have occurred. So, for both Sections 225 and 360:
 - PA has received information that gives PA reason to believe that a SIA is about to be committed or may have occurred.
14. The Task Force did not believe that it would then be sufficient to only require the PA to report the SIA to an appropriate level of management. Doing so would not move current practice beyond the status quo and would result in the Board's efforts in this project falling short of expectations. Instead, the Task Force believes that some element of escalation (to the extent possible), with an evaluation of whether the remedial action was timely and appropriate, would still be necessary to enable the PA to continue to think about whether the PA needs to address the matter further. Therefore, the Task Force believes that it would be necessary for the PA to form a judgment about the appropriateness of the response of management or TCWG, and then consider the appropriate course of action. Guidance could be provided regarding factors the PA could take into account when judging the appropriateness of the response of management or TCWG.

Section 225

For auditors: the matter is related to the client's financial reporting or it falls within the PA's professional expertise, and the matter is significant.

- Refer to the requirements and guidance in ISA 250.

For PAs in public practice providing non-audit services to an audit client: the matter is related to the client's financial reporting or it falls within the PA's professional expertise, and the matter is significant.

- Discuss the matter with the appropriate level of management unless prohibited by applicable law and regulation.
- Consider management's response and if it is not timely or appropriate, escalate within the entity to the extent possible.
- Guidance on factors to consider in judging appropriateness of management's response.

For PAs in public practice providing services to a non-audit client: the matter is related to the subject matter of the professional services being provided by the PA.

- Discuss the matter with the appropriate level of management unless prohibited by applicable law and regulation.
- Consider management's response and if it is not timely or appropriate, escalate within the entity to the extent possible.
- Guidance on factors to consider in judging appropriateness of management's response.

Section 360

For PAIBs: the matter is related to the employing organization's financial reporting, or the subject matter falls within the PA's expertise.

- Discuss the matter with the appropriate level of management unless prohibited by applicable law and regulation.
- Consider management's response and if it is not timely or appropriate, escalate within the entity to the extent possible.
- Guidance on factors to consider in judging appropriateness of management's response.

15. The Task Force believes that the PA's actions thereafter should be left to the PA's judgment. Such an approach would give the PA the flexibility to decide the extent to which the PA would need to be further involved. With Section 140 providing for the possibility of the PA disclosing the SIA to an appropriate authority, guidance could be provided to encourage the PA to consider a range of possible other responses that could be appropriate in the circumstances. For example:

Section 225

For auditors, refer to the possible course of action set out in ISA 250. However, disclosure to an appropriate authority may also be considered (cf s140 on confidentiality).

PAs in public practice providing non-audit services to an audit client should also consider:

- Reporting to TCWG, if not already done so.
- Reporting the matter to the internal audit department, if any.
- Reporting the matter to the audit engagement partner.
- Resignation from the professional relationship where permitted by applicable law or regulation (cf s110 on integrity).
- Disclosure to an appropriate authority (cf s140 on confidentiality).

PAs in public practice providing services to a non-audit client should also consider:

- Reporting to TCWG, if not already done so.
- Reporting the matter to the internal audit department, if any.
- Reporting the matter to the external auditor
- Resignation from the professional relationship where permitted by applicable law or regulation (cf s110 on integrity).
- Disclosure to an appropriate authority (cf s140 on confidentiality).

Section 360

PAIBs should also consider:

- Reporting to TCWG, if not already done so.
- Reporting the matter to the internal audit department, if any.
- Reporting to an ethics hotline or other internal whistle-blowing mechanism.
- Reporting the matter to the external auditor.
- Resignation from the professional relationship where permitted by applicable law or regulation (cf s110 on integrity).
- Disclosure to an appropriate authority (cf s140 on confidentiality).

16. The Task Force believes that making disclosure to an external auditor one of a number of possible responses by PAs as illustrated above would address many of the objections to the ED proposal to require disclosure to the external auditor. Guidance could be provided as to when it may be appropriate to consider reporting to an external auditor.
17. The Task Force acknowledges that a number of aspects of this outline of a possible way forward would need to be further considered, taking into account respondents' significant comments on the ED. Nevertheless, IESBA members are asked to share reactions to this preliminary proposal for a way forward.