

Mr. Ken Siong

Deputy Director

International Ethics Standards Board for Accountants (IESBA)

15 December 2012

Dear Mr. Siong,

Re: FEE comments on IESBA Exposure Draft: “Responding to a Suspected Illegal Act”

- 1 The Malta institute of Accountants (MIA) is pleased to provide you with its comments on the IESBA Exposure Draft “Responding to a Suspected Illegal Act” (“the ED”) with proposed changes to the IESBA Code of Ethics for Professional Accountants (“the Code”).
- 2 The Institute acknowledges that IESBA’s intention underlying the proposals is that the auditor needs to respond to stakeholders’ expectations to “blow the whistle” to competent authorities on clear violations of laws and regulations having a material impact on financial reporting on matters within the remit of the auditor. Yet we do not support most of the overall and detailed proposals in the ED as explained in our main arguments under the “General comments” below.
- 3 Despite our significant concerns with the proposals, we are also providing our responses to the questions which are posed in the ED’s request for specific comments and we have included these as an Appendix to this letter.

- 4 The MIA is not commenting on IESBA's impact assessment and on the proposed changes to the existing sections of the Code.

General comments

- 5 Our main concern is that we do not believe that the matters which the proposed changes are attempting to address should be dealt with in a Code for Professional Accountants. As a Code is not a legal instrument, it cannot provide for protection with respect to the professional accountants' liability, especially as the proposals relate to suspected illegal acts. We propose that, provided that there are safeguards, such matters should be dealt with in legislation and not in a Code for Professional Accountants. Such legislation could provide for the protection of the accountant against legal and other consequences of suspected illegal acts not judged in court to be illegal acts, against allegations of breach of confidentiality and for mitigation of any potential physical threats, safeguards which cannot be offered by a Code.
- 6 The main rationale put forward by the IESBA for the proposals is that the new requirements would be in the public interest. However, from the proposals it is not clear what the public interest is, and auditors/accountants cannot be "judges" of the public interest in the case of suspected illegal acts based on which external reporting to authorities is to be performed, which is eventually for the public courts to decide. Furthermore in many cases, an accountant is not in a position to make subjective judgements about whether a matter is in fact illegal.
- 7 We think that bringing to the auditor's attention information about suspected illegal acts from other accountants who provide other unrelated services to the company and requiring the auditor to then make judgments about the other accountants' information, not only blurs the important lines about what the auditor is auditing but also puts the auditor in a fundamentally unfair position about being the "watchdog" over potentially all aspects of a company's business – whether within the auditor's role and responsibilities or not. It unreasonably extends the auditor's responsibility from what is revealed by the audit process to what is revealed by an accountant outside the firm and at any time.

- 8 The proposal effectively creates a two-tiered ethical system. Indeed, if the company engages an accounting firm to render non-audit services, they will have to adhere to the additional responsibilities imposed by the ED. If in the other hand the same entity engages others, like non-certified / non-chartered consultants, they will be have no such ethical impositions. We think that this will be conducive to creating an uneven playing field that will ultimately place accountants at a competitive disadvantage.

For further information on this MIA¹ letter, please contact Mark Abela on 2258 1900 or on email mabela@miamalta.org.

Yours sincerely,

Anthony Doublet

MIA President

¹ The Malta Institute of Accountants is the voice of the accountancy profession in Malta providing professional guidance, technical support and continuing professional education to over 2,000 accountants.

It is committed to attracting talented individuals to the profession and invests heavily in the process of educating prospective accountants. The MIA also helps to promote a proper understanding of the role and the value of the accountancy profession to the wider Maltese public in general and, in particular, to the local business community.

Appendix- Request for Specific Comments in the IESBA Exposure Draft: “Responding to a Suspected Illegal Act”

The MIA does not support most of the overall and detailed proposals in the Exposure Draft. Our main arguments are presented under the “General comments” above in the covering letter. However, to contribute in a constructive way to the open debate, we are providing some limited but more specific comments in response to the questions which are posed in the ED’s request for specific comments.

Question 1. Do respondents agree that if a professional accountant identifies a suspected illegal act, and the accountant is unable to dispel the suspicion, the accountant should be required to discuss the matter with the appropriate level of management and then escalate the matter to the extent the response is not appropriate? If not, why not and what action should be taken?

9 The MIA agrees that if a professional accountant identifies a suspected illegal act, and the accountant is unable to dispel the suspicion, the accountant should be required to discuss the matter with the appropriate level of management and then escalate the matter to the extent the response is not appropriate.

Question 2. Do respondents agree that if the matter has not been appropriately addressed by the entity, a professional accountant should at least have a right to override confidentiality and disclose certain illegal acts to an appropriate authority?

10 In principle, we would agree with a right (and not an obligation) for a professional accountant to override confidentiality, however subject to the legal provisions in place. Please refer to our general comments.

Question 3. Do respondents agree that the threshold for reporting to an appropriate authority should be when the suspected illegal act is of such consequence that disclosure would be in the public interest? If not, why not and what should be the appropriate threshold?

- 11 In principle, we would agree that when in the professional accountant's opinion, the suspected illegal act is of such consequence that disclosure would be in the public interest, the professional accountant should have a right to disclose, subject to the law provisions in place.
- 12 In addition we do not think that the professional accountant should be expected to exercise this right but that such a matter should best be left to the professional accountant's discretion after having applied his professional judgement.

Question 4. Do respondents agree 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? If not, why not?

- 13 No we do not agree that should be a distinction between the standard for a professional accountant in public practice providing services to an audit client and the standard for a professional accountant in public practice providing services to a client that is not an audit client and we think that there is no justification in the ED for proposing different requirements. We think that International Standards on Auditing (ISAs) are sufficient to cover any circumstances relating to audit.

Question 5. Do respondents agree that an auditor should be required to override confidentiality and disclose certain suspected illegal acts to an appropriate authority if the entity has not made adequate disclosure within a reasonable period of time after being advised to do so? If not, why not and what action should be taken?

- 14 No we do not support this requirement.
- 15 We think that this requirement is in contradiction with the relationship based on trust built between the auditor and his client. We think that the threat of the external reporting of suspected illegal acts by the accountant or auditor might seriously hamper building up trust in their relationship with the client or their employer and the subsequent sharing of information and cooperation.
- 16 We also think that this requirement will create an uneven playing field between professions. In our view this requirement would be outside the remit of the profession and it would be much better that such a requirement was enacted in legislation and constructed in a way where all professionals would be acting in the same way or all professionals delivering the same or similar services were subject to same requirements.

Question 6. Do respondents agree that a professional accountant providing professional services to an audit client of the firm or a network firm should have the same obligation as an auditor? If not, why not and what action should be taken?

- 17 Yes, we generally agree that a professional accountant providing professional services to an audit client of the firm or a network firm should have the same obligation as an auditor.

Question 7. Do respondents agree that the suspected illegal acts to be disclosed referred to in question 5 should be those that affect the client's financial reporting, and acts the subject matter of which falls within the expertise of the professional accountant? If not, why not and which suspected illegal acts should be disclosed?

18 We think that the suspected illegal acts to be disclosed would be those that satisfy both conditions simultaneously, that is, those suspected illegal acts that affect both the client's financial reporting AND acts the subject matter of which falls within the expertise of the professional accountant.

Question 8. Do respondents agree that a professional accountant providing professional services to a client that is not an audit client of the firm or a network firm who is unable to escalate the matter within the client should be required to disclose the suspected illegal act to the entity's external auditor, if any? If not, why not and what action should be taken?

19 We do not agree that a professional accountant should be required to disclose the suspected illegal act to the entity's external auditor. It is unclear to us what the external auditors would then be required to do with such information.

Q9. Do respondents agree that a professional accountant providing professional services to a client that is not an audit client of the firm or a network firm should have a right to override confidentiality and disclose certain illegal acts to an appropriate authority and be expected to exercise this right? If not, why not and what action should be taken?

20 In principle, we would agree that when in the professional accountant's opinion, the suspected illegal act is of such consequence that disclosure would be in the public interest, the professional accountant should have a right to disclose, subject to the law provisions in place.

- 21 However we do not think that the professional accountant should be expected to exercise this right but that such a matter should best be left to the professional accountant's discretion after having applied his professional judgement.

Question 10. Do respondents agree that the suspected illegal acts to be disclosed referred to in question 9 should be those acts that relate to the subject matter of the professional services being provided by the professional accountant? If not, why not and which suspected illegal acts should be disclosed?

- 22 We think that the suspected illegal acts to be disclosed would be those that satisfy both conditions simultaneously, that is, those suspected illegal acts that relate to the subject matter of the professional services being provided by the professional accountant AND those acts that affect the client's financial reporting.

Question 11. Do respondents agree that a professional accountant in business who is unable to escalate the matter within the client or who has doubts about the integrity of management should be required to disclose the suspected illegal act to the entity's external auditor, if any? If not, why not and what action should be taken?

- 23 In principle, we would agree that a professional accountant in business who is unable to escalate the matter within the client or who has doubts about the integrity of management should have a right to disclose the suspected illegal act to the entity's external auditor. However we do not think that the professional accountant should be expected to exercise this right but that such a matter should best be left to the professional accountant's discretion after having applied his professional judgement.
- 24 We note that ISA 240, which sets out the auditor's responsibilities relating to fraud in an audit of financial statements, already requires that the auditor shall make enquires of management to determine whether they have knowledge of any actual, suspected or alleged fraud affecting the entity. We would expect an entity's chief financial officer to be part of senior management and as such would be included within this requirement. However we would not expect more junior members of the accounting team to be part of this requirement.

Question 12. Do respondents agree that a professional accountant in business should have a right to override confidentiality and disclose certain illegal acts to an appropriate authority and be expected to exercise this right? If not, why not and what action should be taken?

- 25 In principle, we would agree that a professional accountant in business should have a right to override confidentiality and disclose certain illegal acts to an appropriate authority, subject to the law provisions in place.
- 26 However we do not think that the professional accountant should be expected to exercise this right but that such a matter should best be left to the professional accountant's discretion after having applied his professional judgement.

Question 13. Do respondents agree that the suspected illegal acts to be disclosed referred to in question 12 above should be acts that affect the employing organization's financial reporting, and acts the subject matter of which falls within the expertise of the professional accountant? If not, why not and which suspected illegal acts should be disclosed?

- 27 We think that the suspected illegal acts to be disclosed would be those that satisfy both conditions simultaneously, that is, those suspected illegal acts that affect both the client's financial reporting AND acts the subject matter of which falls within the expertise of the professional accountant.

Question 14. Do respondents agree 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? If not, why not and what action should be taken?

- 28 Please see our answer to question 12.

Question 15. If respondents agree 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, are the exceptional circumstances as described in the proposal appropriate? If not, how should the exceptional circumstances be described?

29 Please see our answer to question 12.

Question 16. Do respondents agree with the documentation requirements? If not, why not and what documentation should be required?

30 We agree with the documentation requirements proposed. However our agreement should not be interpreted as in any way contradicting our opinion expressed under the general comments section and elsewhere in our comment letter, but that in line with auditing standards and good practice we agree that the auditor should be documenting the results of the work and actions that he would be required to carry out as a result of the ED.