

29 December 2012

Submitted electronically to kensiong@ifac.org

Mr K Siong
Acting Deputy Director
International Ethics Standards Board for Accountants (IESBA)
529 Fifth Avenue, 6th Floor
New York, NY 10017, USA

Dear Ken,

**Comments on the Proposed Change to the Code of Ethics for Professional Accountants
“Responding to a Suspected Illegal Act”**

The Independent Regulatory Board for Auditors (IRBA) is the audit regulator and national auditing and ethics standard setter in South Africa. Its statutory Committee for Auditor Ethics (CFAE) is responsible for prescribing standards of professional competence, ethics and conduct of registered auditors. The IRBA has as one of its statutory objectives the protection of the public by regulating audits performed by registered auditors, and the promotion of investment and employment in South Africa.

The IRBA adopted Parts A and B of the International Ethics Standards Board for Accountants’ (IESBA) *Code of Ethics for Professional Accountants* (the Code), prescribed as the *Code of Professional Conduct for Registered Auditors* (the IRBA Code), in South Africa in 2010 with certain additional national requirements. The IRBA Code together with its *Rules Regarding Improper Conduct* provides the basis for disciplinary action against registered auditors. Consequently, any changes proposed to the IESBA Code that enhances the quality of audits performed by registered auditors and contributes to the integrity of international markets, is of particular interest to the IRBA.

We appreciate this opportunity to comment on the *Proposed Change to the Code of Ethics for Professional Accountants “Responding to a Suspected Illegal Act”* developed by the IESBA. Please accept my apologies for our late submission. I hope you will still be able to take account of our comments considering the far reaching proposals contained in these proposed amendments.

Our comments are presented in the following sections:

- General comments
- Specific comments and responses

If you have any questions or would like to discuss the matters in our comments, please contact Sandy van Esch on: +27 87 940 8871 or at svanesch@irba.co.za.

Yours sincerely

Sandy van Esch
Director: Standards

General comments

1. The proposed amendments to the IESBA Code of Ethics for Professional Accountants (the “IESBA Code”) are drafted in the context of “professional accountants in public practice providing professional services to an audit client” and “professional accountants in business”. Our responses are provided in the context of requirements that the IESBA Code might seek to impose on professional accountants in public practice (in South Africa – this applies to registered auditors) appointed to perform audits and provide other professional services to any entity.
2. Consequently, our specific comments are restricted to the proposed amendments to sections: 100, 140, 150 and 210 and the proposed new section 225 as they pertain to professional accountants in public practice providing professional services to an audit client. Accordingly we do not comment on the proposed amendments to sections 300 and 360 of the IESBA Code as we have no jurisdiction to regulate professional accountants in business. Our more general comments follow.

Legislated requirements vs. Code requirements

3. We have a concern that, unless individual jurisdictions have established legal processes for professional accountants in public practice who becomes aware of a “suspected illegal act”, to report the suspected illegal act to an appropriate regulator that has the power and authority, in the circumstances of the suspected illegal act reported, to investigate and take enforcement action against those involved, the proposed amendments to the Code, may not be implemented or enforceable. We appreciate that this concern is acknowledged on pages 8 and 9 of the Explanatory Memorandum where factors supporting a “right to disclose” rather than a “requirement to disclose” are presented. As a regulator, the IRBA supports the proposal in principle, for auditors in public practice, to have a requirement to report suspected illegal acts but has reservations with regard to some of the proposed changes to the Code.
4. It is advisable for any such legislation to incorporate protective mechanisms for professional accountants in public practice who report such suspected illegal acts in good faith, and which are not reported maliciously. Where such protective mechanisms is not incorporated into legislation, professional accountants who report suspected illegal acts, potentially face litigation from their audit clients against those professional accountants reporting suspected illegal acts resulting in considerable legal costs involved and possible threats to the personal safety of individual professional accountants. The proposed amendments to the IESBA Code cannot offer any legal protection for a professional accountant or auditor who reports a suspected illegal activity and it is unlikely that any Code of Ethics can provide such protection or indemnity if not addressed by relevant legislation in the jurisdiction.
 - 4.1. We are aware that in our jurisdiction, where the auditor responsible for the audit engagement has a statutory responsibility to report reportable irregularities to the IRBA for onward reporting to the relevant Regulator, the indemnity provision contained in the Public Accountants’ and Auditors’ Act, 1951 that preceded our current Auditing Profession Act, 2005 (the Act) was removed. In spite of the statutory responsibility that an auditor has, that is brought to the attention of all audit clients in the auditor’s engagement letter, auditors who identify and report reportable irregularities frequently experience pressure from audit clients, either by way of threats of litigation, of the firm being removed as the auditor, or the individual auditor being

removed as the engagement partner responsible for the engagement, and undue harassment of the auditor and the engagement team completing the audit.

- 4.2. Concerns are expressed that whistleblowing legislation in different jurisdictions may not provide adequate protection for auditors or professional accountants reporting suspected illegal activities to an appropriate regulator.

Nature and materiality of the suspected illegal act

5. The nature of “suspected illegal acts” that are to be reported need to be more clearly defined, as the basis suggested is very broad. Any enforcement action by an appropriate regulator will almost certainly be only in respect of those suspected illegal acts that have caused, or are likely to cause, material financial loss to the entity, or any partner, member, shareholder, creditor or investor of an entity in relation to his or her or its dealings with that entity. The nature and materiality of the impact of a suspected illegal act will form the basis for determining the possible impact on the public interest. The appropriate response by an auditor is set out in the reporting requirements in ISA 250 (paragraphs 25 to 28) which address the appropriate disclosures in the audited financial statements and onward reporting by the auditor to an appropriate regulator. The IESBA Code should align its provisions with ISA 250. Such reporting by a professional accountant or auditor may give rise to legal action being taken by the appropriate regulator, or aggrieved persons, against the parties involved.

- 5.1. Non-compliance with the myriad of legislation and requirements by any entity does not necessarily amount to an intentional “suspected illegal act”, but may result in fines or penalties being levied which, if material, may affect disclosures in the financial statements; and

- 5.2. In the case of global companies operating in many different jurisdictions, the complexity of the laws and regulations applicable to an audit client are such that the professional accountant may be unaware of suspected illegal acts by the entity and where the suspected illegal acts arise from sophisticated intentional illegal acts by management, or those charged with governance, may be extremely difficult for a professional accountant or auditor to detect at an audit client of the firm or network firm.

Parties involved in suspected illegal acts

6. The question of “who” is suspected of being complicit in a suspected illegal act at an entity is also of relevance, whether the individual/s are at a management level, those charged with governance, or a lower level employee is an issue. Different categories of employees, or those charged with governance in an entity, may have a greater or lesser responsibility and authority for taking action to detect and prevent suspected illegal acts by the entity, by management or any other individual employed by the entity. Generally management will be expected to take appropriate action against other employees involved in suspected illegal acts.

- 6.1. For example, where an entity has controls in place to detect suspected illegal acts, and discovers an employee suspected of being so involved and management (including for e.g. a professional accountant in business acting as the CFO) takes action promptly on discovery to sanction the employee and recover any losses that might be incurred, it seems unnecessary to

suggest that such suspected illegal acts have to be reported by the auditor to any appropriate regulator. Where, however, management takes no action to sanction the employee or recover losses incurred, they may be regarded as condoning the actions of the employee and negligent in performance of their fiduciary responsibilities. In such circumstances, the auditor who becomes aware of the suspected illegal act and believes the actions are intentional and material, has a responsibility to communicate with those charged with governance and considers the material effect on the financial statements and whether to communicate to regulatory and enforcement authorities.¹

6.2. Where the professional accountant, or auditor, suspects that management, or those charged with governance, are complicit in the suspected illegal acts, this is clearly more serious, with the inherent risk of override of preventative controls and combined with the possible impact of material financial loss caused to the entity or any partner, member, shareholder, creditor or investor. Knowledge of a suspected illegal act at an audit client may come to the professional accountant's, or auditor's knowledge, from any source, internal or external to the entity. In such circumstances a professional accountant appointed as the auditor complies with the requirements in ISA 250 (paragraphs 22-28) and any additional legislative requirements to report to an appropriate regulator.

7. A further consideration is the nature of professional services provided by the professional accountant. Where an audit of financial statements is conducted in accordance with IAASB International Standards on Auditing (ISAs), or the applicable auditing standards in various jurisdictions, it may reasonably be expected that the auditor complies with ISA 250, has an "audit knowledge" of the client and where he or she "has reason to believe that a material suspected illegal act has, or is likely to have, occurred", considers whether it might materially affect the audited financial statements.

7.1. Where a professional accountant provides other professional services to an audit client, that are permitted in terms of the independence requirements if the IESBA Code, the services provided may be of such a nature that the professional accountant may have little or no chance of detecting a suspected illegal act. Where those services are provided by professional staff at the audit firm who are not professional accountants, they may not have sufficient understanding of the audit client to recognise a suspected illegal act that has, or is likely to have, occurred, or be able to identify the possible parties who are suspected of being complicit in the suspected illegal acts.

Requirements for auditors and independent reviewers to report irregularities

8. Individual registered auditors appointed to perform an audit of any entity, who are satisfied or has reason to believe that a reportable irregularity, as defined in the Act has taken place or is taking place in respect of that entity, have a statutory duty in terms of section 45 of the Act to send a

¹ The auditor's responsibilities to respond appropriately to instances of non-compliance with laws and regulations by the entity, that may include suspected illegal acts, are clarified in ISA 250 *Consideration of Laws and Regulations in an Audit of Financial Statements*. ISA 250 (paragraphs 22 to 28) provide guidance in reporting of identified or suspected non-compliance, including to those charged with governance, disclosure in the auditor's report on the financial statements and reporting to regulatory and enforcement authorities.

written report of the reportable irregularity to the IRBA without delay after detecting the irregularity and determining that it is reportable.

- 8.1. The first reportable irregularity report must contain sufficient detail of the reportable irregularity to enable identification of the appropriate regulator responsible for enforcement of such irregularity (suspected illegal act) for onward transmission by the IRBA to that regulator. The auditor is required to submit a copy of the first reportable irregularity report to a full board of management, including those charged with governance, within 3 days of submitting the report to the IRBA. The auditor then provides management with a reasonable opportunity to respond to the report. Thereafter the auditor sends a second report to the IRBA within 30 days after the first report to confirm: whether the reportable irregularity is or is not continuing, or the suspicions are unfounded and the suspected reportable irregularity did not exist. The Act also provides that an auditor, who “fails to report a reportable irregularity that he or she is satisfied or has reason to believe has taken place or is taking place”, may be subject to a fine or imprisonment or both.
- 8.2. The Act also contains requirements where the second report indicates the reportable irregularity is regarded as continuing, for the auditor’s report on the financial statements of the entity to include under a separate *“Report on other legal and regulatory requirements”* the fact that a reportable irregularity has been reported to the entity. The reportable irregularity reported must be appropriately dealt with by management in the audited financial statements including steps taken by management to address the irregularity disclosed. If this is not done, the auditor is required to disclose information regarding the nature of the reportable irregularity in their auditor’s report. This requirement seeks to address concerns regarding non-disclosure to the public.
- 8.3. Since the introduction of section 45 in the Act effective from 1 April 2006, the IRBA has received approximately 1200 reportable irregularity reports annually. In this way, the IRBA is viewed as contributing to the broader regulatory enforcement mechanisms in the country.
- 8.4. We note the view expressed on page 8 of the Explanatory Memorandum regarding the assumed “low probability of occurrence of illegal acts in smaller entities and expectation that such instances would be rare”. The IRBA’s experience is to the contrary, where approximately 80% of reportable irregularities reported by auditors have been in respect of smaller companies, owner managed businesses and trusts, mainly regarding contraventions of provisions of the Companies Act and often accompanied by income tax or VAT non – compliance, or fraud, or involving misappropriation of employees’ tax deductions or VAT charged not paid to the tax authorities.
- 8.5. The IRBA will consider the final amendments to the IESBA Code for adoption, to the extent considered appropriate, as the Code cannot override the requirements of the Act.
9. The South African Companies Act, 2008 and Regulations, similarly require a professional accountant, including any auditor, who performs an independent review of a company’s financial statements, that is satisfied or has reason to believe that a reportable irregularity has taken place or is taking place in respect of that company, to report without delay to the Companies and Intellectual

Property Commission (CIPC). CIPC exercises their enforcement mechanisms in dealing with reportable irregularities received, which are defined in the Regulations as:

- 9.1. “Any act or omission committed by any person responsible for the management of a company, which:
 - 9.1.1. Unlawfully has or is likely to cause material financial loss to the company, or to a member, shareholder, creditor or investor of the company in respect of his or her dealings with that entity, or
 - 9.1.2. Is fraudulent or amounts to theft; or
 - 9.1.3. Causes or has caused the company to trade in insolvent circumstances.”

Request for Specific Comments

The IESBA would welcome views on the following questions:

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?*

It is difficult to understand how the IESBA Code can seek to impose “requirements” on a professional accountant in public practice that are more demanding than the requirements in the ISAs where the professional accountant is the auditor of an entity and that audit is performed in accordance with the ISAs. The IESBA Code should seek to support and not override the comprehensive ISAs that, for example, set out in ISA 250 the process to be followed by an auditor to consider compliance by the entity with laws and regulations.

An auditor is required to obtain sufficient appropriate evidence to support the auditor’s opinion on the financial statements in complying with the ISAs, and / or other National Auditing Standards applied in the jurisdiction. The ISAs already provide for suspicions regarding non-compliance with laws and regulations by the entity, to be discussed with an appropriate level of management above the level at which a suspected illegal act is identified. A professional accountant, who is not the auditor of the entity, may not have any right of access even to identify, let alone to discuss such suspected illegal acts, with management of an entity at any level.

An auditor also pursues enquiries in the process of gathering sufficient evidence to determine whether or not they have reason to believe that a suspected illegal act has or is likely to have occurred. Formal reporting of a suspected illegal act where this has, or may have, resulted in material losses may be considered a significant matter to be reported to those charged with governance as required by ISA 260 *Communication with those charged with Governance* (paragraph 16).

In circumstances, where there are legislated requirements for reporting of suspected illegal acts other reporting requirements may pertain, for example money laundering legislation that requires such illegal acts to be reported directly to a Financial Intelligence Centre (FIC) to avoid alerting those involved in the suspected illegal act that they have been found out giving them time to cover their tracks and possibly to escape arrest, before the FIC or other legal enforcement processes can

be activated. Such jurisdictional reporting requirements may be imposed by law or a regulator in the first instance on management, followed by those charged with governance of the entity, before requirements are imposed on the auditor.

It is doubtful whether the IESBA Code can succeed in imposing such “requirements” on professional accountants / auditors where these are not required in a particular jurisdiction’s legal and regulatory framework.

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?*

Yes. We agree that, if the matter has not been appropriately addressed by the entity, the professional accountant / auditor of the entity should at least have a right to override confidentiality and disclose certain illegal acts to an appropriate authority after considering all the facts and circumstances, including any confidentiality requirements under local laws and regulations or applicable ISAs and contractual arrangements with the client.

This right may be imposed as a requirement only where there are laws and legal processes in place in a jurisdiction to enable reporting to be made to appropriate regulators. The audit client needs to be made aware of the circumstances when a professional accountant / auditor may have a right, or legal obligation, to override confidentiality. This is best conveyed in the engagement letter with the audit client, stating that such processes and legal obligations are imposed on the professional accountant / auditor of the entity, so that the client is aware of the limitation on the fundamental principle of confidentiality.

Ideally in such circumstances, appropriate protection mechanisms need to be in place for the professional accountant / auditor reporting the suspected illegal act, in good faith, to the appropriate regulator. Failing which, where a suspected illegal act reported is subsequently found not to be illegal, the professional accountant / auditor could face claims for damages for defamation from the audit client.

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?*

Concern has been raised that the definition of “public interest” is too vague and judgmental and insufficient criteria are available to ensure a consistent and objective of the materiality of a suspected illegal act to be established as a threshold for reporting to an appropriate authority. For example, Securities Regulators may have a more narrow perspective focused on the possible impact for investors on misleading price sensitive information, whereas other regulators may have a much broader view of stakeholders whose interests may be materially and adversely impacted by suspected illegal acts by an entity.

The expectation in Section 225.11 that “the auditor consider the number of people that could be affected by the suspected illegal act and extent to which they could be affected” as a threshold, seems largely impractical, and public interest is merely one of the factors to be considered. An auditor may be expected to consider “public interest” as one of the factors, amongst many other

factors, when evaluating the possible impact of suspected illegal acts that have caused, or are likely to cause, “*material financial loss to the entity, or any partner, member, shareholder, creditor or investor of an entity in relation to his or her or its dealings with that entity*” is possible. This latter basis, however, is likely to provide a more consistent basis for determining whether a suspected illegal act should be reported to those charged with governance or an appropriate regulator, since the auditor considers the materiality in the context of that applied in the evaluation of materiality in their audit of the financial statements of the entity.

We consider that reporting should not be limited only to those matters that are viewed as being in the public interest, but extend to those suspected illegal acts that may be criminal or statutory offences. Different jurisdictions are likely to view the concept and “quantum of losses” that are in the “public interest” very differently. In all cases it will require the exercise of professional judgement by the professional accountant / auditor to determine whether or not, and to whom, a suspected illegal act should be reported in the particular circumstances.

Matters specific to professional accountants in public practice (Section 225 of the Code)

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?

We do not agree, however, that there should be any difference in the quality of professional services provided to an audit or non-audit client. A consistently high standard of ethics should be applied by all professional accountants / auditors in accordance with the fundamental principles in the IESBA Code in respect of all professional services provided to the public. The Code is not the appropriate place to seek to set different ethics standards for professional services provided to audit or non-audit clients. The standards required for services provided by professional accountants / auditors to audit and non-audit clients are covered in the IAASB standards for audit, assurance, reviews and related services engagements respectively, or related National Standards in different jurisdictions, that differentiate between the types of services provided

The relationship between the professional accountant / auditor providing audit services to an audit client is quite different from that of a professional accountant / auditor providing other non-audit professional services to a non-audit client.

- Firstly, a professional accountant / auditor who is not the auditor of the entity cannot be assumed to have an audit knowledge of the client and may be quite unaware that a suspected illegal act has, or is likely to have occurred or be able to assess the possible impact from their more narrow perspective. An auditor is required to report on the financial statements of the entity as a whole and is expected to obtain sufficient appropriate evidence to support that opinion. Where a suspected illegal act may exist that could materially affect the financial statements, the auditor complies with the requirements of ISA 250, or the equivalent in the particular jurisdiction and cannot simply ignore any suspicions.
- Secondly, when providing non-audit services to a non-audit client, a professional accountant may not have a right of access to obtain information or to inquire into matters outside of their particular professional engagement, to determine whether or not they do indeed have reason to believe that a suspected illegal act has, or is likely to have occurred, beyond the

particular professional services they are providing. The client will expect that the professional accountant respects the confidentiality of their professional relationship with the entity and this may be included in their contractual arrangements with the client. If the professional accountant seeks to report their suspicions to the auditor of the entity or an appropriate regulator this could result in the client taking legal action against the professional accountant for a breach of contract and given the more limited perspective the professional accountant may have could lead to a misunderstanding regarding the suspected illegal act. Unlike an attorney, where attorney: client privilege is protected, a professional accountant does not enjoy such protection.

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?

No we do not agree that an auditor should be required to override confidentiality and disclose certain suspected illegal acts to an appropriate authority, unless there are legal requirements and established processes in the jurisdiction for an auditor to report suspected illegal acts and a mechanism to identify the appropriate authority (regulator) to whom the auditor should report. Without such legal requirements, it may be difficult to enforce such a requirement in the Code for an auditor, or for an audit regulator to take disciplinary action against an auditor who having considered all the circumstances decides in their professional judgement that the suspected illegal act should not be reported to an appropriate regulator, or the auditor is unable to identify an appropriate regulator to report to.

Consideration should also be given to whether the disclosures in the audited financial statements of the entity regarding material suspected illegal acts are appropriate. The auditor also follows the requirements in ISA 260 for escalating the suspected illegal acts by reporting to those above the level at which the suspected illegal act has been identified and / or to those charged with governance.

Depending on the nature of the suspected illegal act, individual regulators may for example, include in Listing Requirements of a Securities Exchange or in Regulations to the Banks Act, in a particular jurisdiction, specific requirements for an auditor to report all material suspected illegal acts that may materially affect investors or create a systemic risk for the banking industry to the Securities Regulator or Bank Regulator respectively.

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?

Generally agree, however, this will depend on the nature of the professional services provided to the audit client, and the relationship with the network firm.

Ordinarily, a network firm within a jurisdiction that has laws that require an auditor to report suspected illegal acts, will have established internal arrangements for communication to the engagement partner responsible for the audit, of any possible suspected illegal acts identified in the course of providing those other professional services to an audit client. This is not a fool proof

guarantee that all such instances will be communicated, but the professional accountant providing professional services to an audit client may indeed, detect material suspected illegal acts and alert the engagement partner responsible for the audit engagement.

Where however the network firm providing the professional services is located in another jurisdiction they may be quite unaware of the engagement partner's responsibilities to report suspected illegal acts and fail to bring the suspected illegal act to the attention of the audit engagement partner.

Without a global requirement such as that now being proposed as Section 225 of the IESBA Code, and convergence of different jurisdictions' Codes of Ethics with the IESBA Code, network firms in other jurisdictions that are not required to report suspected illegal act to an appropriate regulator, are unlikely to be aware of, or to communicate suspected illegal acts identified to the audit engagement partner in a jurisdiction that does have such requirements.

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?*

Our response to question 5 indicated that we did not agree that suspected illegal acts should be disclosed to an appropriate regulator, unless the jurisdiction has legal requirements and processes imposing that requirement on professional accountant or auditor. A Code cannot impose that responsibility where the jurisdiction's legal and regulatory framework does not require such disclosure.

Having said that, it is most probable that suspected illegal acts that materially affect the financial statements of the entity and auditor's reporting thereon are those more likely to be detected by an auditor and which are most likely to fall within the expertise of a professional accountant / auditor. There is nothing to prevent an auditor whose suspicions are aroused, from obtaining expert advice regarding another more complex or technical suspected illegal act in order to exercise their professional judgement in determining whether or not suspected illegal act has, or is likely to have, occurred.

Suspected illegal acts may affect any aspect of a business and depending on the complexity of the suspected illegal acts that have caused, or are likely to cause, "*material financial loss to the entity, or any partner, member, shareholder, creditor or investor of an entity in relation to his or her or its dealings with that entity*" the evaluation of the possible impact will undoubtedly affect the professional accountant's / auditor's decision whether or not to disclose and the timing thereof:

- to whom such disclosure should be made – whether to management and / or those charged with governance; and / or
- to determine the appropriate regulator to report to, depending on nature of the suspected illegal act and the existence of jurisdictional requirements and established legal processes in this regard; and
- to consider the implications for disclosures by management in the audited financial statements and "regulatory reporting matters" to include in the auditor's report thereon.

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?*

No, we disagree with a requirement imposed on 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, to disclose the matter to the entity's external auditor. This may be one of the possible options a professional accountant may determine is appropriate after due consideration of all relevant facts and circumstances, but should not be imposed as a requirement in the Code.

Moreover, a professional accountant whose firm is not the auditor of the entity and who is unable to escalate the matter within the client may not have sufficient knowledge and understanding of the full circumstances to determine that the alleged acts, are indeed suspected illegal acts. Disclosure of a suspected illegal act to the entity's auditor in such circumstances may be misleading and the professional accountant may then find he or she has violated the Code's confidentiality requirements and is in breach of their contractual engagement responsibilities to the client.

9. *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?*

Whilst agreeing 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, we do not agree that the professional accountant "be expected to exercise this right" as this effectively imposes a requirement. The professional accountant needs to consider all facts and circumstances surrounding the suspected illegal act identified, including the legal and regulatory framework in the jurisdiction before determining the appropriate action to take. Where the professional accountant determines it is appropriate to disclose the suspected illegal act to an appropriate authority, this should not be construed as a violation of the Code's confidentiality requirements.

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?*

Whilst it is likely that a suspected illegal act may be encountered in the course of the professional services being provided, it is possible that a suspected illegal act identified may be in respect of matters that are not related to the professional services being provided. It is recognised that a professional accountant may become aware of a suspected illegal act from any source, not necessarily only from the performance of the professional services being provided.

As indicated in our response to question 9, the professional accountant needs to consider all facts and circumstances surrounding the suspected illegal act identified, including the legal and regulatory framework in the jurisdiction before determining the appropriate action to take.

Matters specific to professional accountants in business (Section 360 of the Code)

As the IRBA does not regulate professional accountants in business we have not commented on the proposed changes to Section 360 in Part C of the IESBA Code.

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?

No Comment

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?

No Comment

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?

No Comment

Other

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?

In the absence of laws or regulations requiring a professional accountant to disclose certain illegal acts to an appropriate authority there are bound to be "exceptional circumstances" when a professional accountant considering all relevant circumstances, determines that they are not required, nor wish to exercise a right, to disclose a suspected illegal act to an appropriate authority.

There will always be an element of doubt whether or not a suspected illegal act will eventually be judged to be illegal when brought to court and all arguments both for and against the allegations are heard and considered. Consequently, a professional accountant has to weigh up all factors, including the personal risk of threats to life and limb of the professional accountant, the engagement team and any family members. In such circumstances, the professional accountant cannot be regarded as being in violation of the Code.

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?

It is inappropriate to try to provide an exhaustive list of possible exceptions in a Code, one can merely establish the principle and it will then be up to the facts of the circumstances to be

considered. Sections 225.14 and 225.20 appear to adequately describe such circumstances. Clearly in such circumstances the professional accountant / auditor reconsiders their client and engagement acceptance and continuance procedures as set out in Section 210 of the Code and determines whether or not to terminate the engagement and client relationship.

We do not agree with the suggestion in Section 225.14 that the professional accountant considers whether it is “appropriate to provide professional services in the particular jurisdiction”. The fact that a particular client relationship and engagement is discontinued does not appear to be grounds for discontinuing the professional accountant’s public practice in a particular jurisdiction.

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

Currently the only documentation requirements in the Code are contained in Sections 290.29 and 291.29 that recognise documentation provides evidence of threats and safeguards considered and the auditor’s or professional accountant’s conclusions in meeting the Independence Requirements in the Code.

The proposed Section 225.23 documentation requirements in the first two sentences seem appropriate to document the steps taken to establish the nature and materiality of suspected illegal acts and that support the professional accountant’s / auditor’s determination of disclosures to be made management, those charged with governance, in the financial statements and reported to an appropriate authority.

However, the extensive “requirements” for documentation where the professional accountant determines that a suspected illegal act is not disclosed to an appropriate regulator seem excessive unless there is a legal or regulatory requirement for the professional accountant to report suspected illegal acts. The last bullet point that appears almost nonsensical.

17. Do respondents agree with the proposed changes to the existing sections of the Code? If not, why not and what changes should be made?

The final proposed changes to:

- Section 100 still to come from the earlier proposed changes to the Code to address ethical conflicts of interest are not reflected, so it is difficult to determine whether further changes are necessary;
- Section 100.21: the proposed deletion of the final two sentences will depend on the final proposed wording of the proposed new Section 225;
- Section 140.7 and 140.8 (v): No comment subject to other general comments to be considered in finalising the proposed new Section 225;
- Section 150.1: completely disagree – “suspected illegal acts” are completely different from “unethical acts” and should not be used interchangeably; and
- Section 210.2 and 201.5: disagree with the proposed changes - “suspected illegal acts” are completely different from “unethical acts” and should not be used interchangeably.

We have expressed several serious reservations in our comments above with regard to the proposed changes imposing a requirement, or the extending the right, of a professional accountant to override confidentiality principles in order to disclose suspected illegal acts identified at an entity that is an audit client or at a non-audit client, to an appropriate authority.

This suggests that the IESBA needs to re-consider the proposed amendments and may require additional research and possibly re-exposure before finalising amendments to the Code that may not be possible to implement, or may be unenforceable in a Code as this may mitigate against convergence in some jurisdictions.

- Without legal or regulatory requirements in a jurisdiction, that require reporting of suspected illegal acts to an appropriate authority or regulator it is unlikely that the proposed changes, beyond the requirements to communicate to management or those charged with governance will be implemented ;
- In addition, unless suitable protection (indemnity) is provided for professional accountants / auditors who report suspected illegal acts in good faith, in the course of their audit or other professional services provided, they may be exposed to legal action taken against them by their clients.

18. Do respondents agree with the impact analysis as presented? Are there any other stakeholders, or other impacts on stakeholders, that should be considered and addressed by the IESBA

We find the impact analysis of limited use and have concerns that the far reaching implications have not been fully considered, nor due regard being had to implementation in those jurisdictions that do not have a regulatory and enforcement framework, that supports disclosures to an appropriate regulator, and provides indemnity to a professional accountant / auditor who discloses suspected illegal acts in good faith.

The public interest implications have not been clearly articulated.