

RESPONDING TO NON-COMPLIANCE WITH LAWS OR REGULATIONS— STRAW MAN

[Note: The changes to Sections 100, 140 and 150 shown in mark-up below are proposed changes to the extant Code. Sections 225 and 360 are new sections.]

SECTION 100

Introduction and Fundamental Principles

...

Fundamental Principles

100.5 A professional accountant shall comply with the following fundamental principles:

...

- (e) Professional Behavior – to comply with relevant laws and regulations and avoid any action-conduct that discredits the profession.

...

SECTION 140

Confidentiality

140.1 The principle of confidentiality imposes an obligation on all professional accountants to refrain from:

- (a) Disclosing outside the firm or employing organization confidential information acquired as a result of professional and business relationships without proper and specific authority or unless there is a legal or professional right or duty to disclose; and
- (b) Using confidential information acquired as a result of professional and business relationships to their personal advantage or the advantage of third parties.

140.2 A professional accountant shall maintain confidentiality, including in a social environment, being alert to the possibility of inadvertent disclosure, particularly to a close business associate or a close or immediate family member.

140.3 A professional accountant shall maintain confidentiality of information disclosed by a prospective client or employer.

140.4 A professional accountant shall maintain confidentiality of information within the firm or employing organization.

140.5 A professional accountant shall take reasonable steps to ensure that staff under the professional accountant's control and persons from whom advice and assistance is obtained respect the professional accountant's duty of confidentiality.

140.6 The need to comply with the principle of confidentiality continues even after the end of relationships between a professional accountant and a client or employer. When a professional accountant changes employment or acquires a new client, the professional accountant is

entitled to use prior experience. The professional accountant shall not, however, use or disclose any confidential information either acquired or received as a result of a professional or business relationship.

Circumstances Where Confidential Information May be Disclosed

140.7 ~~The following~~ As a fundamental principle, confidentiality serves the public interest because it facilitates the free flow of information between a professional accountant and the professional accountant's client or employer. Nevertheless, there are circumstances where the professional accountants ~~are~~ is or may be required to disclose confidential information, or when such disclosure may be appropriate.

140.8 A professional accountant may override the duty of confidentiality when:

- (a) Disclosure is required by law ~~or regulation, for example:~~
- (b) There is a professional duty or right to disclose, when not prohibited by law ~~or regulation; or:~~
- (c) Disclosure is permitted by law and is authorized by the client or the employer.

140.9 Circumstances where disclosure is required by law or regulation may include, for example:

- (i) Production of documents or other 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.~~

140.10 A professional accountant has a professional duty or right to disclose, when not prohibited by law or regulation, to:

- (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 and ethics standards, such as when disclosing identified or suspected non-compliance with laws or regulations to an appropriate authority in the circumstances described in Sections 225 and 360.

140.811 In deciding whether to disclose confidential information, relevant factors to consider include:

- Whether the interests of ~~all~~ any parties, including third parties whose interests may be affected, could be harmed if the client or employer consents to the disclosure of information by the professional accountant.
- Whether all the relevant information is known and substantiated, to the extent it is practicable; when the situation involves unsubstantiated facts, incomplete information or unsubstantiated conclusions, professional judgment shall be used in determining the type of disclosure to be made, if any.
- The type of communication that is expected and to whom it is addressed.
- Whether the parties to whom the communication is addressed are appropriate recipients.

SECTION 150

Professional Behavior

- 150.1 The principle of professional behavior imposes an obligation on all professional accountants to comply with relevant laws and regulations and avoid any ~~action-conduct~~ that the professional accountant knows or should know may discredit the profession. This includes actions or other conduct that a reasonable and informed third party, weighing all the specific facts and circumstances available to the professional accountant at that time, would be likely to conclude adversely affects the good reputation of the profession. Such conduct includes not responding to circumstances where the professional accountant has identified or suspects non-compliance with laws or regulations by a client or an employer.
- 150.2 In marketing and promoting themselves and their work, professional accountants shall not bring the profession into disrepute. Professional accountants shall be honest and truthful and not:
- (a) Make exaggerated claims for the services they are able to offer, the qualifications they possess, or experience they have gained; or
 - (b) Make disparaging references or unsubstantiated comparisons to the work of others.

PROPOSED SECTION 225

Responding to Identified or Suspected Non-Compliance with Laws or Regulations

- 225.1 This section addresses the responsibilities of a professional accountant in public practice when the professional accountant identifies or suspects that non-compliance with laws or regulations by a client has occurred or may be about to occur. For the purposes of this section, non-compliance comprises acts of omission or commission, intentional or unintentional, committed by a client, or by those charged with governance, management or employees of a client which are contrary to the prevailing laws or regulations, for example, fraud. Personal misconduct unrelated to the business activities of the client and matters that are clearly inconsequential are excluded. Whether an act constitutes non-compliance with laws or regulations is ultimately a matter for legal determination by a court of law.

Responsibilities of the Client or Its Management

- 225.2 It is the responsibility of the client or its management, with the oversight of those charged with governance, to ensure that the client's business activities are conducted in accordance with laws and regulations. It is also the responsibility of the client, its management and those charged with governance, to address any non-compliance with laws or regulations by the client or by those charged with governance, management or employees of the client.

Responsibilities of Professional Accountants in Public Practice

- 225.3 In some jurisdictions, there are legal or regulatory requirements governing how identified or suspected non-compliance with laws or regulations is to be addressed. If so, the professional accountant shall comply with those requirements, including with respect to any prohibitions on alerting ("tipping-off") the client prior to making any disclosure, for example, pursuant to anti-money laundering legislation.

Obtaining an Understanding of the Matter

- 225.4 If a professional accountant becomes aware in the course of performing a professional service for a client of information concerning an instance of non-compliance or suspected non-compliance with laws or regulations, including where the instance of non-compliance may be about to occur, the professional accountant shall seek to obtain an understanding of the nature of the matter and the circumstances in which it arose. In seeking to obtain such an understanding, the professional accountant shall endeavor to gather relevant information available to make an assessment. The professional accountant is expected to apply knowledge, judgment and expertise, but is not expected to have detailed knowledge of laws and regulations beyond that which is required for the professional service for which the accountant was engaged.
- 225.5 With respect to a professional accountant performing a non-audit service for a non-audit client, the professional accountant may have become aware of the matter during the course of the engagement, but it may not necessarily be within the professional accountant's expertise. The closer the matter is to the professional accountant's expertise, the greater the duty for the professional accountant to pursue the matter with the client.

- 225.6 The professional accountant may consult with others within the firm, a network firm, a relevant professional body, or legal counsel to:
- Understand the application of the relevant laws and regulations to the circumstances and whether the act is potentially contrary to laws or regulations;
 - Assess the gravity of the matter;
 - Understand the potential consequences of the matter to the client, including the impact on the client's financial reporting; and
 - Identify the possible courses of action.
- 225.7 If the professional accountant is performing a non-audit service for an audit client of the firm, or a network firm, the professional accountant shall discuss the matter with the engagement partner for the audit in order that the audit engagement team is made appropriately aware of the matter and a determination can be made of how the matter should be addressed in accordance with the provisions of this section.
- 225.8 If the professional accountant identifies or suspects non-compliance with laws or regulations, the professional accountant shall discuss the matter with the client to:
- (a) Confirm the professional accountant's understanding of the facts and circumstances relevant to the matter, and the potential consequences of the matter; and
 - (b) Understand what actions the client, its management or those charged with governance plan to take to address the matter, including whether they plan to disclose it to an appropriate authority.
- 225.9 The professional accountant shall undertake such discussions with the appropriate level of management and, where appropriate, those charged with governance. The determination of which level of management is the appropriate level with whom to discuss the instance of non-compliance with laws or regulations is a question of professional judgment. Relevant factors to consider include:
- The nature of the matter.
 - The circumstances and individuals involved.
 - The likelihood of collusion.
 - The gravity of the matter.
 - Whether that level of management is able to take action to investigate the matter and take remedial action.
- 225.10 The appropriate level of management is generally at least one level above the person or persons who appear to be involved in the matter. In the context of an audit engagement, if the professional accountant suspects that management or those charged with governance are involved in the non-compliance, the professional accountant shall discuss the matter with the next higher level of authority at the entity, if it exists, such as an audit committee or supervisory board. The professional accountant may also consider discussing the matter with internal auditors, where applicable. In the context of a group audit engagement, the appropriate level may be management at an entity that controls the client. Where no higher authority exists, or if

the professional accountant believes that the communication may not be acted upon or is unsure as to the person to whom to report, the professional accountant is encouraged to obtain legal advice.

- 225.11 The professional accountant shall assess whether the client, its management or those charged with governance understand their legal or regulatory responsibilities with respect to the matter and, if not, may recommend that they obtain legal advice.
- 225.12 If insufficient information is obtained to satisfy the professional accountant that the client is in compliance with laws and regulations, the professional accountant shall consider the need to obtain legal advice regarding possible actions to take.

Evaluating the Response of the Client

- 225.13 The professional accountant shall evaluate whether the client, its management or those charged with governance have appropriately addressed the matter. In so doing, the professional accountant shall consider the nature and gravity of the matter and factors such as whether:
- The matter has been adequately investigated.
 - Action has been taken to remediate the matter.
 - Appropriate steps have been taken to reduce the risk of re-occurrence, for example, additional controls or training.
 - The matter has been disclosed to an appropriate authority where appropriate and, if so, whether the disclosure appears adequate.
- 225.14 The degree to which the professional accountant is able to evaluate the response of the client, its management or those charged with governance may vary with the nature of the professional services provided to the client. In particular, if the client is an audit client, the professional accountant generally has greater access to information and management, by law or otherwise, than if the client is not an audit client.
- 225.15 If the client is an audit client and, in the professional accountant's judgment, the response of the client is not appropriate or the professional accountant is unable to assess whether the response is appropriate, the professional accountant shall:
- (a) Inform those charged with governance; and
 - (b) Consider the professional accountant's reporting responsibilities under auditing standards.
- The professional accountant may also consider consulting with a relevant professional body or seeking legal advice.
- 225.16 If the client is not an audit client and, in the professional accountant's judgment, the response of the client is not appropriate or the professional accountant is unable to assess whether the response is appropriate, the professional accountant shall consider:
- (a) Informing those charged with governance;
 - (b) Alerting the external auditor, if any, to the matter to enable the external auditor to determine whether specific action is needed in the context of the audit; or

- (c) Seeking advice from the professional accountant's professional body or seeking legal advice.

225.17 If, in the professional accountant's opinion, the client has not appropriately addressed the matter or if the professional accountant is unable to assess whether the response is appropriate, the professional accountant shall determine whether to disclose the matter to an appropriate authority in accordance with paragraphs 225.18-225.24.

Disclosing Non-Compliance with Laws or Regulations to an Appropriate Authority

225.18 Where there is no legal or regulatory requirement to disclose the non-compliance to an appropriate authority, and to do so is not contrary to law or regulation in the relevant jurisdiction, the professional accountant shall consider whether voluntary disclosure to an appropriate authority is appropriate. A distinguishing mark of the accountancy profession is its acceptance of the responsibility to act in the public interest. Accordingly, a professional accountant is permitted to override the duty of confidentiality under this Code by disclosing identified or suspected non-compliance with laws or regulations to an appropriate authority where, in the professional accountant's judgment, such disclosure would be in the public interest.

225.19 In determining whether disclosure would be in the public interest, the professional accountant shall evaluate the gravity of the matter, for example, the consequences to those potentially affected by the matter in both financial and non-financial terms, including the nature and extent of any damage to the wider public.

225.20 In determining whether or not to disclose identified or suspected non-compliance with laws or regulations to an appropriate authority, the professional accountant shall also consider the following:

- The degree to which the relevant information is known and substantiated.
- Whether there is an appropriate authority to receive the information. An appropriate authority is one with responsibility for such a matter. In many instances, that authority will have the ability to investigate and take action to safeguard the public interest. The appropriate authority to which to disclose the matter will depend on the nature of the matter, for example, a competition regulator in the case of cartel arrangements, and a securities regulator in the case of fraudulent financial reporting.
- Whether there is protection from civil or criminal liability afforded by legislation or regulation, such as under whistle-blowing legislation or regulation.

225.21 The professional accountant is encouraged to seek legal advice to understand the legal implications of disclosure to an appropriate authority.

225.22 When the professional accountant has determined that disclosure would in principle be in the public interest and the client is a public interest entity audit client, there is a presumption that the professional accountant will disclose the matter to an appropriate authority when the following conditions are met:

- (a) The matter has a material impact on the financial statements and the financial statements have not been adjusted to reflect that impact;

- (b) There is an appropriate authority to receive the information;
- (c) The client has not already adequately disclosed the matter to the appropriate authority;
and
- (d) There is protection afforded by legislation or regulation, for example, under whistle-blowing legislation or regulation which is sufficiently established to protect the professional accountant from civil and criminal liability.

Paragraph 225.26 specifies the documentation required where the auditor of a public interest entity concludes that the presumption is not applicable in the circumstances and, accordingly, does not disclose the matter to an appropriate authority.

- 225.23 When making a disclosure to an appropriate authority, and thus overriding the fundamental principle of confidentiality, the professional accountant shall act in good faith and exercise caution when making statements and assertions. The professional accountant shall also consider whether it is appropriate to inform the client of the professional accountant's intentions before making such disclosure.
- 225.24 The professional accountant may also consider withdrawing from the engagement and the professional relationship where permitted by law or regulation. Withdrawal, however, is not a substitute for complying with this section.

Documentation

- 225.25 The professional accountant is encouraged to document the nature and substance of the matter, the details of discussions held, and the decisions made concerning the matter. Documentation provides a number of benefits, including the following:
- It provides evidence of the professional accountant's judgments in forming conclusions.
 - It may serve to protect the professional accountant if challenged in legal or disciplinary proceedings to justify the professional accountant's actions in responding to the matter.
 - It may assist the professional accountant if required to appear before a court of law or tribunal to provide testimony regarding the matter.
- 225.26 If, when acting as the auditor of a public interest entity, a professional accountant has concluded that the presumption specified in paragraph 225.22 is not applicable in the circumstances, the professional accountant shall document the reasons for that conclusion.

PROPOSED SECTION 360

Responding to Identified or Suspected Non-Compliance with Laws or Regulations

360.1 This section addresses the responsibilities of a professional accountant in business when the professional accountant identifies or suspects that non-compliance with laws or regulations by an employing organization has occurred or may be about to occur. For the purposes of this section, non-compliance comprises acts of omission or commission, intentional or unintentional, committed by an employing organization, or by those charged with governance, management or employees of an employing organization which are contrary to the prevailing laws or regulations, for example, fraud. Personal misconduct unrelated to the business activities of the employing organization and matters that are clearly inconsequential are excluded. Whether an act constitutes non-compliance with laws or regulations is ultimately a matter for legal determination by a court of law.

Responsibilities of the Employing Organization and Its Management

360.2 It is the responsibility of the employing organization and its management, with the oversight of those charged with governance, to ensure that the employing organization's business activities are conducted in accordance with laws and regulations. It is also the responsibility of the employing organization, its management and those charged with governance, to address any non-compliance with laws or regulations by the employing organization or by those charged with governance, management or employees of the employing organization.

Responsibilities of Professional Accountants in Business

360.3 In some jurisdictions, there are legal or regulatory requirements governing how identified or suspected non-compliance with laws or regulations is to be addressed. If so, the professional accountant shall comply with those requirements.

Obtaining an Understanding of the Matter

360.4 If a professional accountant becomes aware in the course of carrying out the professional accountant's employment responsibilities of information concerning an instance of non-compliance or suspected non-compliance with laws or regulations, including where the instance of non-compliance may be about to occur, the professional accountant shall seek to obtain an understanding of the nature of the matter and the circumstances in which it arose. In seeking to obtain such an understanding, the professional accountant shall endeavor to gather relevant information available to make an assessment. The professional accountant is expected to apply knowledge, judgment and expertise, but is not expected to have detailed knowledge of laws and regulations beyond that which is required for the professional activity the accountant is undertaking. While the professional accountant may have become aware of the matter when carrying out the professional accountant's employment responsibilities, it may not necessarily be within the professional accountant's expertise. The closer the matter is to the professional accountant's expertise, the greater the duty for the professional accountant to pursue the matter with the employer.

360.5 The professional accountant shall consider the protocols and procedures, if any, that have been established by the employing organization to address such a matter (for example, an ethics policy).

- 360.6 The professional accountant may consult with a relevant professional body or legal counsel to:
- Understand the application of the relevant laws and regulations to the circumstances and whether the act is potentially contrary to law or regulation;
 - Assess the gravity of the matter;
 - Understand the potential consequences of the matter to the employing organization; and
 - Identify the possible courses of action.
- 360.7 If the professional accountant identifies or suspects non-compliance with laws or regulations, the professional accountant shall generally first address the matter within the reporting lines of the employing organization by discussing the matter with an immediate superior or higher levels of management as deemed appropriate in the circumstances. The purposes of this discussion are to:
- (a) Confirm the professional accountant's understanding of the facts and circumstances relevant to the matter, and the potential consequences of the matter; and
 - (b) Understand what actions the immediate superior, management or those charged with governance plan to take to address the matter, including whether they plan to disclose it to an appropriate authority.
- 360.8 Professional accountants in business can be involved in a variety of roles involving the preparation and reporting of financial information as well as general management activities. Employing organizations rely on their expertise to help ensure that the business activities are undertaken in accordance with relevant laws and regulations. Accordingly, the professional accountant shall assess whether management or those charged with governance understand their legal or regulatory responsibilities with respect to the matter and, if not, may recommend that the employing organization obtain legal advice.
- 360.9 If insufficient information is obtained to satisfy the professional accountant that the employing organization is in compliance with laws and regulations, the professional accountant shall consider the need to obtain legal advice regarding possible actions to take.
- 360.10 In certain circumstances, the professional accountant may deem it more appropriate to communicate the matter in accordance with the protocols established by the employing organization's ethics policy where such protocols allow for anonymity, rather than discussing the matter with an immediate superior or higher levels of management. This may be appropriate when the professional accountant is employed in a relatively junior position and believes that the non-compliance is deliberate and involves different layers of management. This will enable the matter to be rapidly escalated to those best able to address it.

Evaluating the Response of Management or Those Charged with Governance

- 360.11 The professional accountant shall evaluate whether the professional accountant's immediate superior, management or those charged with governance have taken appropriate remedial action. In so doing, the professional accountant shall consider the nature and gravity of the matter and factors such as whether:
- The matter has been adequately investigated;

- Action has been taken to remediate the matter;
 - Appropriate steps have been taken to reduce the risk of re-occurrence, such as for example, additional controls or training; and
 - The matter has been disclosed to an appropriate authority where appropriate and, if so, whether the disclosure appears adequate.
- 360.12 If, in the professional accountant's judgment, the response to the matter is not appropriate, or the professional accountant suspects that the immediate superior or management is involved in the non-compliance, or the professional accountant is unable to assess whether the response is appropriate, the professional accountant shall:
- (a) Escalate the matter within the entity, for example with higher levels of management, internal audit, or those charged with governance;
 - (b) Disclose the matter in accordance with any established mechanism such as an ethics policy; or
 - (c) Disclose the matter to the employing organization's external auditor, if any, to enable the auditor to determine appropriate actions in the context of the external audit.
- 360.13 If the professional accountant is unable to escalate the matter, or if the professional accountant has doubts about the integrity or honesty of management and those charged with governance and there is no established mechanism such as an ethics policy, the professional accountant shall consider discussing the matter with a relevant professional body or legal counsel.
- 360.14 If, in the professional accountant's opinion, management or those charged with governance have not taken the remedial action the professional accountant considers appropriate in the circumstances, the professional accountant shall determine whether to disclose the matter to an appropriate authority in accordance with paragraphs 360.15-360.20.

Disclosing Non-Compliance with Laws or Regulations to an Appropriate Authority

- 360.15 Where there is no legal or regulatory requirement to disclose non-compliance to an appropriate authority, and to do so is not contrary to law or regulation in the relevant jurisdiction, the professional accountant shall consider whether voluntary disclosure to an appropriate authority is appropriate. A distinguishing mark of the accountancy profession is its acceptance of the responsibility to act in the public interest. Accordingly, a professional accountant is permitted to override the duty of confidentiality under this Code by disclosing identified or suspected non-compliance with laws or regulations to an appropriate authority where, in the professional accountant's judgment, such disclosure would be in the public interest.
- 360.16 In determining whether disclosure would be in the public interest, the professional accountant shall evaluate the gravity of the matter, for example, the consequences to those potentially affected by the matter in both financial and non-financial terms, including the nature and extent of any damage to the wider public.
- 360.17 In determining whether or not to disclose identified or suspected non-compliance with laws or regulations to an appropriate authority, the professional accountant shall also consider the following:
- The degree to which the relevant information is known and substantiated.

- Whether there is an appropriate authority to receive the information. An appropriate authority is one with responsibility for such a matter. In many instances, that authority will have the ability to investigate and take action to safeguard the public interest. The appropriate authority to which to disclose the matter will depend upon the nature of the matter, for example, a competition regulator in the case of cartel arrangements, and a securities regulator in the case of fraudulent financial reporting.
- Whether there is protection from civil or criminal liability afforded by legislation or regulation, such as under whistle blowing legislation or regulation.

360.18 The professional accountant is encouraged to seek legal advice to understand the legal implications of disclosure to an appropriate authority.

360.19 When making a disclosure to an appropriate authority, and thus overriding the fundamental principle of confidentiality, the professional accountant shall act in good faith and exercise caution when making statements and assertions.

360.20 The professional accountant may also consider resigning from the employing organization. Resignation, however, is not a substitute for complying with this section.

Documentation

360.21 The professional accountant is encouraged to document the nature and substance of the matter, the details of discussions held, and the decisions made concerning the matter. Documentation provides a number of benefits, including the following:

- It provides evidence of the professional accountant's judgments in forming conclusions.
- It may serve to protect the professional accountant if challenged in legal or disciplinary proceedings to justify the professional accountant's actions in responding to the matter.
- It may assist the professional accountant if required to appear before a court of law or tribunal to provide testimony regarding the matter.