

**NOCLAR—Proposed Section 360
(Clean)****Responding to Non-Compliance with Laws and Regulations****Introduction**

- 360.1 Professional accountants are required to comply with the fundamental principles and apply the conceptual framework set out in Section 120 to identify, evaluate and address threats.
- 360.2 Threats to compliance with the principles of integrity and professional behavior are created when an accountant becomes aware of an act or suspected act of non-compliance with laws and regulations.
- 360.3 Section 360 sets out requirements and application material regarding the approach to be taken by a professional accountant when responding to non-compliance or suspected non-compliance with:
- (a) Laws and regulations generally recognized to have a direct effect on the determination of material amounts and disclosures in the client's financial statements; and
 - (b) Other laws and regulations that do not have a direct effect on the determination of the amounts and disclosures in the client's financial statements, but compliance with which might be fundamental to the operating aspects of the client's business, to its ability to continue its business, or to avoid material penalties.

Requirements and Application Material**General**

- 360.4 A1 Non-compliance with laws and regulations ("non-compliance") comprises acts of omission or commission, intentional or unintentional, which are contrary to the prevailing laws or regulations committed by the following parties:
- (a) A client;
 - (b) Those charged with governance;
 - (c) Management; or
 - (d) Other individuals working for or under the direction of a client.
- 360.4 A2 Examples of laws and regulations which this section addresses include those that deal with:
- Fraud, corruption and bribery.
 - Money laundering, terrorist financing and proceeds of crime.
 - Securities markets and trading.
 - Banking and other financial products and services.
 - Data protection.

- Tax and pension liabilities and payments.
- Environmental protection.
- Public health and safety.

R360.5 The professional accountant shall apply this section regardless of the nature of the client, including whether or not it is a public interest entity.

360.5 A1 A professional accountant might encounter or be made aware of non-compliance or suspected non-compliance with laws and regulations in the course of providing a professional service to a client. This section guides the accountant in assessing the implications of the matter and the possible courses of action when responding to it.

R360.6 In some jurisdictions, there are legal or regulatory provisions governing how professional accountants should address non-compliance or suspected non-compliance. These legal or regulatory provisions might differ from or go beyond the provisions in this section. When encountering such non-compliance or suspected non-compliance, the accountant shall obtain an understanding of those legal or regulatory provisions and comply with them, including:

- (a) Any requirement to report the matter to an appropriate authority; and
- (b) Any prohibition on alerting the client prior to making any disclosure.

360.6 A1 A prohibition on alerting the client prior to making any disclosure might arise, for example, pursuant to anti-money laundering legislation.

360.7 A1 A distinguishing mark of the accountancy profession is its acceptance of the responsibility to act in the public interest. When responding to non-compliance or suspected non-compliance, the objectives of the professional accountant are:

- (a) To comply with the principles of integrity and professional behavior;
- (b) By alerting management or, where appropriate, those charged with governance of the client, to seek to:
 - (i) Enable them to rectify, remediate or mitigate the consequences of the identified or suspected non-compliance; or
 - (ii) Deter the commission of the non-compliance where it has not yet occurred; and
- (c) To take such further action as appropriate in the public interest.

360.7 A2 Non-compliance might result in fines, litigation or other consequences for the client, potentially materially affecting its financial statements. Importantly, such non-compliance might have wider public interest implications in terms of potentially substantial harm to investors, creditors, employees or the general public. For the purposes of this section, an act that causes substantial harm is one that results in serious adverse consequences to any of these parties in financial or non-financial terms. Examples include the perpetration of a fraud resulting in significant financial losses to investors, and breaches of environmental laws and regulations endangering the health or safety of employees or the public.

360.7 A3 A professional accountant who encounters or is made aware of matters that are clearly inconsequential is not required to comply with this section. Whether a matter is clearly inconsequential is to be judged with respect to its nature and its impact, financial or otherwise, on the client, its stakeholders and the general public.

360.7 A4 This section does not address:

- (a) Personal misconduct unrelated to the business activities of the client; and
- (b) Non-compliance by parties other than those specified in paragraph 360.4 A1. This includes, for example, circumstances where a professional accountant has been engaged by a client to perform a due diligence assignment on a third party entity and the identified or suspected non-compliance has been committed by that third party.

The accountant might nevertheless find the guidance in this section helpful in considering how to respond in these situations.

Responsibilities of the Client’s Management and Those Charged with Governance

360.8 A1 Management, with the oversight of those charged with governance, is responsible for ensuring that the client’s business activities are conducted in accordance with laws and regulations. Management and those charged with governance are also responsible for identifying and addressing any non-compliance by:

- (a) The client;
- (b) An individual charged with governance of the entity;
- (c) A member of management; or
- (d) Other individuals working for or under the direction of the client.

Responsibilities of Professional Accountants

R360.9 Where a professional accountant becomes aware of a matter to which this section applies, the steps that the accountant takes to comply with this section shall be taken on a timely basis. In taking timely steps, the accountant shall have regard to the nature of the matter and the potential harm to the interests of the entity, investors, creditors, employees or the general public.

Audits of Financial Statements

Obtaining an Understanding of the Matter

R360.10 If a professional accountant engaged to perform an audit of financial statements becomes aware of information concerning an instance of non-compliance or suspected non-compliance, the accountant shall obtain an understanding of the matter. This understanding shall include the nature of the act and the circumstances in which it has occurred or might occur.

360.10 A1 The professional accountant might become aware of the instance of non-compliance or suspected non-compliance in the course of performing the engagement or through information provided by other parties.

- 360.10 A2 The professional accountant is expected to apply knowledge and expertise, and exercise professional judgment. However, the accountant is not expected to have a level of knowledge of laws and regulations greater than that which is required to undertake the engagement. Whether an act constitutes non-compliance is ultimately a matter to be determined by a court or other appropriate adjudicative body.
- 360.10 A3 Depending on the nature and significance of the matter, the professional accountant might consult on a confidential basis with others within the firm, a network firm or a professional body, or with legal counsel.
- R360.11** If the professional accountant identifies or suspects that non-compliance has occurred or might occur, the accountant shall discuss the matter with the appropriate level of management and, where appropriate, those charged with governance.
- 360.11 A1 The purpose of the discussion is to clarify the professional accountant's understanding of the facts and circumstances relevant to the matter and its potential consequences. The discussion also might prompt management or those charged with governance to investigate the matter.
- 360.11 A2 The appropriate level of management with whom to discuss the matter is a question of professional judgment. Relevant factors to consider include:
- The nature and circumstances of the matter.
 - The individuals actually or potentially involved.
 - The likelihood of collusion.
 - The potential consequences of the matter.
 - Whether that level of management is able to investigate the matter and take appropriate action.
- 360.11 A3 The appropriate level of management is usually at least one level above the individual or individuals involved or potentially involved in the matter. In the context of a group, the appropriate level might be management at an entity that controls the client.
- 360.11 A4 The professional accountant might also consider discussing the matter with internal auditors, where applicable.
- R360.12** If the professional accountant believes that management is involved in the non-compliance or suspected non-compliance, the accountant shall discuss the matter with those charged with governance.

Addressing the Matter

- R360.13** In discussing the non-compliance or suspected non-compliance with management and, where appropriate, those charged with governance, the professional accountant shall advise them to take appropriate and timely actions, if they have not already done so, to:
- (a) Rectify, remediate or mitigate the consequences of the non-compliance;
 - (b) Deter the commission of the non-compliance where it has not yet occurred; or

- (c) Disclose the matter to an appropriate authority where required by law or regulation or where considered necessary in the public interest.

R360.14 The professional accountant shall consider whether the client’s management and those charged with governance understand their legal or regulatory responsibilities with respect to the non-compliance or suspected non-compliance.

360.14 A1 If management and those charged with governance do not understand their legal or regulatory responsibilities with respect to the matter, the professional accountant might suggest appropriate sources of information or recommend that they obtain legal advice.

R360.15 The professional accountant shall comply with applicable:

- (a) Laws and regulations, including legal or regulatory provisions governing the reporting of non-compliance or suspected non-compliance to an appropriate authority; and
- (b) Requirements under auditing standards, including those relating to:
- Identifying and responding to non-compliance, including fraud.
 - Communicating with those charged with governance.
 - Considering the implications of the non-compliance or suspected non-compliance for the auditor’s report.

360.15 A1 Some laws and regulations might stipulate a period within which reports of non-compliance or suspected non-compliance are to be made to an appropriate authority.

Communication with Respect to Groups

R360.16 Where a professional accountant becomes aware of non-compliance or suspected non-compliance in relation to a component of a group in either of the following two situations, the accountant shall communicate the matter to the group engagement partner unless prohibited from doing so by law or regulation:

- (a) The accountant is, for purposes of an audit of the group financial statements, requested by the group engagement team to perform work on financial information related to the component; or
- (b) The accountant is engaged to perform an audit of the component’s financial statements for purposes other than the group audit, for example, a statutory audit.

The communication to the group engagement partner shall be in addition to responding to the matter in accordance with the provisions of this section,

360.16 A1 The purpose of the communication is to enable the group engagement partner to be informed about the matter and to determine, in the context of the group audit, whether and, if so, how to address it in accordance with the provisions in this section.

R360.17 Where the group engagement partner becomes aware of non-compliance or suspected non-compliance in the course of an audit of group financial statements, the group engagement partner shall consider whether the matter might be relevant to one or more components:

- (a) Whose financial information is subject to work for purposes of the audit of the group financial statements; or
- (b) Whose financial statements are subject to audit for purposes other than the group audit, for example, a statutory audit.

This consideration shall be in addition to responding to the matter in the context of the group audit in accordance with the provisions of this section.

R360.18 If the non-compliance or suspected non-compliance might be relevant to one or more of the components specified in paragraph R360.17(a) and (b), the group engagement partner shall take steps to have the matter communicated to those performing work at the components, unless prohibited from doing so by law or regulation.

If necessary, the group engagement partner shall arrange for appropriate inquiries to be made as to whether the relevant component(s) specified in paragraph R360.17(b) is subject to audit and, if so, to ascertain to the extent practicable the identity of the auditor.

360.18 A1 The purpose of the communication is to enable those responsible for work at the components to be informed about the matter and to determine whether and, if so, how to address it in accordance with the provisions in this section.

360.18 A2 For the components specified in paragraph R360.17(b), the inquiries might be made either of management or from publicly available information.

Determining Whether Further Action Is Needed

R360.19 The professional accountant shall assess the appropriateness of the response of management and, where applicable, those charged with governance.

360.19 A1 Relevant factors to consider in assessing the appropriateness of the response of management and, where applicable, those charged with governance include whether:

- The response is timely.
- The non-compliance or suspected non-compliance has been adequately investigated.
- Action has been, or is being, taken to rectify, remediate or mitigate the consequences of any non-compliance.
- Action has been, or is being, taken to deter the commission of any non-compliance where it has not yet occurred.
- Appropriate steps have been, or are being, taken to reduce the risk of re-occurrence, for example, additional controls or training.
- The non-compliance or suspected non-compliance has been disclosed to an appropriate authority where appropriate and, if so, whether the disclosure appears adequate.

R360.20 In light of the response of management and, where applicable, those charged with governance, the professional accountant shall determine if further action is needed in the public interest.

- 360.20 A1 The determination of whether further action is needed, and the nature and extent of it, will depend on various factors, including:
- The legal and regulatory framework.
 - The urgency of the situation.
 - The pervasiveness of the matter throughout the client.
 - Whether the professional accountant continues to have confidence in the integrity of management and, where applicable, those charged with governance.
 - Whether the non-compliance or suspected non-compliance is likely to recur.
 - Whether there is credible evidence of actual or potential substantial harm to the interests of the entity, investors, creditors, employees or the general public.
- 360.20 A2 Examples of circumstances that might cause the professional accountant no longer to have confidence in the integrity of management and, where applicable, those charged with governance include situations where:
- The accountant suspects or has evidence of their involvement or intended involvement in any non-compliance.
 - The accountant is aware that they have knowledge of such non-compliance and, contrary to legal or regulatory requirements, have not reported, or authorized the reporting of, the matter to an appropriate authority within a reasonable period.
- R360.21** The professional accountant shall exercise professional judgment in determining the need for, and nature and extent of, further action. In making this determination, the accountant shall take into account whether a reasonable and informed third party would be likely to conclude that the accountant has acted appropriately in the public interest.
- 360.21 A1 Further action that the professional accountant might take includes:
- Disclosing the matter to an appropriate authority even when there is no legal or regulatory requirement to do so.
 - Withdrawing from the engagement and the professional relationship where permitted by law or regulation.
- 360.21 A2 Withdrawing from the engagement and the professional relationship is not a substitute for taking other actions that might be needed to achieve the professional accountant's objectives under this section. In some jurisdictions, however, there might be limitations as to the further actions available to the accountant. In such circumstances, withdrawal might be the only available course of action.
- R360.22** Where the professional accountant has withdrawn from the professional relationship pursuant to paragraphs R360.20 and 360.21 A1, the accountant shall, on request by the proposed successor accountant, provide all such facts and other information concerning the identified or suspected non-compliance to the proposed successor accountant. The predecessor accountant shall do so despite paragraph R320.11, unless prohibited by law or regulation.

360.22 A1 The facts and other information to be provided are those that, in the predecessor accountant's opinion, the proposed successor accountant needs to be aware of before deciding whether to accept the audit appointment. Section 320 addresses communications from proposed successor accountants.

R360.23 If the proposed successor accountant is unable to communicate with the predecessor accountant, the proposed successor accountant shall take reasonable steps to obtain information about the circumstances of the change of appointment by other means.

360.23 A1 Other means to obtain information about the circumstances of the change of appointment include inquiries of third parties or background investigations of management or those charged with governance.

360.24 A1 As consideration of the matter might involve complex analysis and judgments, the professional accountant might consider:

- Consulting internally.
- Obtaining legal advice to understand the accountant's options and the professional or legal implications of taking any particular course of action.
- Consulting on a confidential basis with a regulator or professional body.

Determining Whether to Disclose the Matter to an Appropriate Authority

360.25 A1 Disclosure of the matter to an appropriate authority would be precluded if doing so would be contrary to law or regulation. Otherwise, the purpose of making disclosure is to enable an appropriate authority to cause the matter to be investigated and action to be taken in the public interest.

360.25 A2 The determination of whether to make such a disclosure depends in particular on the nature and extent of the actual or potential harm that is or might be caused by the matter to investors, creditors, employees or the general public. For example, the professional accountant might determine that disclosure of the matter to an appropriate authority is an appropriate course of action if:

- The entity is engaged in bribery (for example, of local or foreign government officials for purposes of securing large contracts).
- The entity is regulated and the matter is of such significance as to threaten its license to operate.
- The entity is listed on a securities exchange and the matter might result in adverse consequences to the fair and orderly market in the entity's securities or pose a systemic risk to the financial markets.
- It is likely that the entity would sell products that are harmful to public health or safety.
- The entity is promoting a scheme to its clients to assist them in evading taxes.

360.25 A3 The determination of whether to make such a disclosure will also depend on external factors such as:

- Whether there is an appropriate authority that is able to receive the information, and cause the matter to be investigated and action to be taken. The appropriate authority will depend on the nature of the matter. For example, the appropriate authority would be a securities regulator in the case of fraudulent financial reporting or an environmental protection agency in the case of a breach of environmental laws and regulations.
- Whether there exists robust and credible protection from civil, criminal or professional liability or retaliation afforded by legislation or regulation, such as under whistle-blowing legislation or regulation.
- Whether there are actual or potential threats to the physical safety of the professional accountant or other individuals.

R360.26 If the professional accountant determines that disclosure of the non-compliance or suspected non-compliance to an appropriate authority is an appropriate course of action in the circumstances, this is not a breach of the duty of confidentiality under Subsection 114 of the Code. When making such disclosure, the accountant shall act in good faith and exercise caution when making statements and assertions. The accountant shall also consider whether it is appropriate to inform the client of the accountant's intentions before disclosing the matter.

R360.27 In exceptional circumstances, the professional accountant might become aware of actual or intended conduct that the accountant has reason to believe would constitute an imminent breach of a law or regulation that would cause substantial harm to investors, creditors, employees or the general public. In these circumstances, the accountant shall exercise professional judgment and may immediately disclose the matter to an appropriate authority in order to prevent or mitigate the consequences of such imminent breach. Such disclosure is not a breach of the duty of confidentiality under Subsection 114 of the Code.

360.27 A1 Prior to deciding whether to disclose the matter to an appropriate authority immediately, the professional accountant might consider whether it would be appropriate to discuss the matter with management or those charged with governance of the entity.

Documentation

R360.28 In relation to an identified or suspected act of non-compliance that falls within the scope of this section, the professional accountant shall document:

- How management and, where applicable, those charged with governance have responded to the matter.
- The courses of action the accountant considered, the judgments made and the decisions that were taken, having regard to the reasonable and informed third party concept.
- How the accountant is satisfied that the accountant has fulfilled the responsibility set out in paragraph R360.20.

- 360.28 A1 This documentation is in addition to complying with the documentation requirements under applicable auditing standards. *International Standards on Auditing (ISAs)*, for example, require a professional accountant performing an audit of financial statements to:
- Prepare documentation sufficient to enable an understanding of significant matters arising during the audit, the conclusions reached, and significant professional judgments made in reaching those conclusions;
 - Document discussions of significant matters with management, those charged with governance, and others, including the nature of the significant matters discussed and when and with whom the discussions took place; and
 - Document identified or suspected non-compliance, and the results of discussion with management and, where applicable, those charged with governance and other parties outside the entity.

Professional Services Other than Audits of Financial Statements

Obtaining an Understanding of the Matter and Addressing It with Management and Those Charged with Governance

- R360.29** If a professional accountant engaged to provide a professional service other than an audit of financial statements becomes aware of information concerning an instance of non-compliance or suspected non-compliance, the accountant shall seek to obtain an understanding of the matter. This understanding shall include the nature of the act and the circumstances in which it has occurred or might be about to occur.
- 360.29 A1 The professional accountant is expected to apply knowledge and expertise, and exercise professional judgment. However, the accountant is not expected to have a level of understanding of laws and regulations beyond that which is required for the professional service for which the accountant was engaged. Whether an act constitutes actual non-compliance is ultimately a matter to be determined by a court or other appropriate adjudicative body.
- 360.29 A2 Depending on the nature and significance of the matter, the professional accountant might consult on a confidential basis with others within the firm, a network firm or a professional body, or with legal counsel.
- R360.30** If the professional accountant identifies or suspects that non-compliance has occurred or might occur, the accountant shall discuss the matter with the appropriate level of management. If the accountant has access to those charged with governance, the accountants shall also discuss the matter with them where appropriate.
- 360.30 A1 The purpose of the discussion is to clarify the professional accountant's understanding of the facts and circumstances relevant to the matter and its potential consequences. The discussion also might prompt management or those charged with governance to investigate the matter.
- 360.30 A2 The appropriate level of management with whom to discuss the matter is a question of professional judgment. Relevant factors to consider include:
- The nature and circumstances of the matter.

- The individuals actually or potentially involved.
- The likelihood of collusion.
- The potential consequences of the matter.
- Whether that level of management is able to investigate the matter and take appropriate action.

Communicating the Matter to the Entity's External Auditor

R360.31 If the professional accountant is performing a non-audit service for:

- (a) An audit client of the firm; or
- (b) A component of an audit client of the firm,

the accountant shall communicate the non-compliance or suspected non-compliance within the firm, unless prohibited from doing so by law or regulation. The communication shall be made in accordance with the firm's protocols or procedures. In the absence of such protocols and procedures, it shall be made directly to the audit engagement partner.

R360.32 If the professional accountant is performing a non-audit service for:

- (a) An audit client of a network firm; or
- (b) A component of an audit client of a network firm,

the accountant shall consider whether to communicate the non-compliance or suspected non-compliance to the network firm. Where the communication is made, it shall be made in accordance with the network's protocols or procedures. In the absence of such protocols and procedures, it shall be made directly to the audit engagement partner.

R360.33 If the professional accountant is performing a non-audit service for a client that is not:

- (a) An audit client of the firm or a network firm; or
- (b) A component of an audit client of the firm or a network firm,

the accountant shall consider whether to communicate the non-compliance or suspected non-compliance to the firm that is the client's external auditor, if any.

360.34 A1 Factors relevant to considering the communication in accordance with paragraphs R360.32 to R360.33 include:

- Whether doing so would be contrary to law or regulation.
- Whether there are restrictions about disclosure imposed by a regulatory agency or prosecutor in an ongoing investigation into the non-compliance or suspected non-compliance.
- Whether the purpose of the engagement is to investigate potential non-compliance within the entity to enable it to take appropriate action.
- Whether management or those charged with governance have already informed the entity's external auditor about the matter.

- The likely materiality of the matter to the audit of the client's financial statements or, where the matter relates to a component of a group, its likely materiality to the audit of the group financial statements.

360.35 A1 In the circumstances addressed in paragraphs R360.31 to R360.33, the purpose of the communication is to enable the audit engagement partner to be informed about the non-compliance or suspected non-compliance and to determine whether and, if so, how to address it in accordance with the provisions of this section.

Considering Whether Further Action Is Needed

R360.36 The professional accountant shall also consider whether further action is needed in the public interest.

360.36 A1 Whether further action is needed, and the nature and extent of it, will depend on factors such as:

- The legal and regulatory framework.
- The appropriateness and timeliness of the response of management and, where applicable, those charged with governance.
- The urgency of the situation.
- The involvement of management or those charged with governance in the matter.
- The likelihood of substantial harm to the interests of the client, investors, creditors, employees or the general public.

360.36 A2 Further action by the professional accountant might include:

- Disclosing the matter to an appropriate authority even when there is no legal or regulatory requirement to do so.
- Withdrawing from the engagement and the professional relationship where permitted by law or regulation.

360.36 A3 In considering whether to disclose to an appropriate authority, relevant factors to take into account include:

- Whether doing so would be contrary to law or regulation.
- Whether there are restrictions about disclosure imposed by a regulatory agency or prosecutor in an ongoing investigation into the non-compliance or suspected non-compliance.
- Whether the purpose of the engagement is to investigate potential non-compliance within the entity to enable it to take appropriate action.

R360.37 If the professional accountant determines that disclosure of the non-compliance or suspected non-compliance to an appropriate authority is an appropriate course of action in the circumstances, this is not a breach of the duty of confidentiality under Subsection 114 of the Code. When making such disclosure, the accountant shall act in good faith and exercise caution when making statements and assertions. The accountant shall also

consider whether it is appropriate to inform the client of the accountant's intentions before disclosing the matter.

R360.38 In exceptional circumstances, the professional accountant might become aware of actual or intended conduct that the accountant has reason to believe would constitute an imminent breach of a law or regulation that would cause substantial harm to investors, creditors, employees or the general public. In these circumstances, the accountant shall exercise professional judgment and may immediately disclose the matter to an appropriate authority in order to prevent or mitigate the consequences of such imminent breach of law or regulation. Such disclosure is not a breach of the duty of confidentiality under Subsection 114 of the Code.

360.38 A1 Prior to deciding whether to disclose the matter to an appropriate authority immediately, the professional accountant might consider whether it would be appropriate to discuss the matter with management or those charged with governance of the entity.

360.39 A1 The professional accountant might consider:

- Consulting internally.
- Obtaining legal advice to understand the professional or legal implications of taking any particular course of action.
- Consulting on a confidential basis with a regulator or professional body.

Documentation

360.40 A1 In relation to an identified or suspected act of non-compliance that falls within the scope of this section, the professional accountant is encouraged to document:

- The matter.
- The results of discussion with management and, where applicable, those charged with governance and other parties.
- How management and, where applicable, those charged with governance have responded to the matter.
- The courses of action the accountant considered, the judgments made and the decisions that were taken.
- How the accountant is satisfied that the accountant has fulfilled the responsibility set out in paragraph R360.36.