



## STAFF QUESTIONS &amp; ANSWERS

[JANUARY 2017]

## RESPONDING TO NON-COMPLIANCE WITH LAWS AND REGULATIONS

### *Professional Accountants in Business*

#### **(CLEAN)**

This Questions and Answers (Q&A) publication is issued by the Staff of the International Ethics Standards Board for Accountants® (IESBA®). It is intended to assist national standards setters, IFAC member bodies and professional accountants (PAs) in public practice (including firms) as they adopt and implement the provisions in Section 360<sup>1</sup> of the IESBA *Code of Ethics for Professional Accountants™* (the Code) addressing PAs' responsibility to respond to non-compliance with laws and regulations (NOCLAR). The IESBA issued its [NOCLAR pronouncement](#) in July 2016.

This publication does not amend or override the Code, the text of which alone is authoritative. Reading the Q&As is not a substitute for reading the Code. The Q&As are not intended to be exhaustive and reference to the Code itself should always be made.<sup>2</sup> This publication does not constitute an authoritative or official pronouncement of the IESBA.

#### I. **General**

##### **Nature of Section 360**

- Q1.** Is Section 360 only general guidance or does it impose any obligation on the PAIB in circumstances where the PAIB becomes aware of NOCLAR or suspected NOCLAR?
- A.** Section 360 is not merely guidance for the PAIB to follow at the PA's discretion. It contains a number of requirements with which the PAIB must comply. These requirements (designated by the word "shall") vary between "senior PAIBs" as described in paragraph 360.13 and other PAIBs. Where the matter is within the scope of Section 360, an overriding obligation under the Code is for the PAIB to respond to it and not simply ignore it.

<sup>1</sup> Section 360, *Responding to Non-Compliance with Laws and Regulations*

<sup>2</sup> References to the Code in this publication are to the Code extant as of the date of this publication. The Code can be accessed at: <http://www.ethicsboard.org/iesba-code>.

## Interaction with Laws and Regulations

**Q2.** In jurisdiction X, there are legal provisions governing how PAs should address certain types of NOCLAR, including a requirement to report NOCLAR or suspected NOCLAR to designated public authorities. If a PAIB has complied with these provisions with respect to NOCLAR or suspected NOCLAR within the scope of Section 360, does this mean that the PAIB need not comply with the rest of Section 360?

**A.** No. Reporting of NOCLAR or suspected NOCLAR to an appropriate authority is only one aspect of Section 360, and it is subject to any confidentiality laws that may exist in the particular jurisdiction (see in particular paragraph 360.28 of the Code). Section 360 contains other provisions that would apply if not already required or prohibited by law or regulation. These include, for example, provisions addressing escalation of the matter within the employing organization; mitigation or remediation of the consequences of NOCLAR or the deterrence of NOCLAR; and resignation from the employing organization.

In addition, the Preface to the Code states that some jurisdictions may have legal, regulatory or professional requirements and guidance that differ from those contained in this Code. It emphasizes that PAs in those jurisdictions need to be aware of those differences and comply with whichever are the more stringent requirements and guidance unless prohibited from doing so by law or regulation.

**Q3.** Jurisdiction X has confidentiality laws that prohibit PAs from disclosing NOCLAR or suspected NOCLAR to an appropriate authority. Does this mean that the NOCLAR provisions in the Code have limited applicability or relevance in that jurisdiction?

**A.** First and foremost, PAIBs must comply with all applicable laws and regulations, including laws prohibiting the disclosure of confidential information. However, if PAIBs are prohibited from complying with certain parts of the Code by law or regulation, they still need to comply with all other parts of the Code. Accordingly, all the other NOCLAR provisions in Section 360 would still apply to the extent that compliance with them is not prohibited by law or regulation. See also Q2.

Further, in the case of groups with components in other parts of the world, application of the NOCLAR provisions of the Code in the jurisdictions where those components are based might have implications and relevance in jurisdiction X. For example, PAIBs in a management or governance role at the parent entity in jurisdiction X might have to consider and address the implications for the parent entity and the group arising from the disclosure of NOCLAR or suspected NOCLAR by the auditor of a component to a public authority in another jurisdiction.

## Scope

### *Nature of NOCLAR*

**Q4.** A PAIB becomes aware of a breach of a law by an entity with which the PAIB has no employment relationship, whether contractual or otherwise. Does the PAIB have any responsibility to respond to the matter under Section 360 of the Code?

- A. No. As the PAIB has no employment relationship with the entity and is otherwise not working under the direction of the entity, Section 360 does not apply. The PAIB would be in the same position as an ordinary good citizen in those circumstances.
- Q5. Does the Code require PAIBs to respond to acts of NOCLAR committed by contractors or agents working for the employing organization, or by non-executive directors of the employing organization?
- A. Yes. Paragraph 360.2 of the Code defines NOCLAR to include acts committed by individuals working for or under the direction of the employing organization which are contrary to prevailing laws or regulations. Contractors, agents and non-executive directors are examples of parties who work for or under the direction of an employing organization. In the context of responding to NOCLAR under the Code, it is not necessary that there be a formal employment relationship between the party that has committed the act of NOCLAR and the organization, as might be established through an employment contract.

#### *Clearly Inconsequential Matters*

- Q6. Why does Section 360 (paragraph 360.8) scope out clearly inconsequential matters when paragraph 360.5 already indicates that laws and regulations covered are those that directly affect the determination of *material* amounts and disclosures in the financial statements, and those in respect of which compliance may be *fundamental* to the employing organization's business?
- A. The phrases "*material* amounts and disclosures" and "*fundamental* to the operating aspects of the business" used to describe the laws and regulations within the scope of Section 360 refer to the kind of laws and regulations this Section is concerned about (see paragraph 360.6 for examples). These phrases are not referring to actual instances of NOCLAR or suspected NOCLAR. For example, laws and regulations addressing corporate taxation are within the scope of Section 360. However, a small fine for narrowly missing a deadline for filing the employing organization's tax return would be a clearly inconsequential matter which the PAIB need not pursue under the Code.

#### **Identifying NOCLAR**

- Q7. Paragraph 360.1 indicates that a PAIB may encounter or be made aware of NOCLAR or suspected NOCLAR in the course of carrying out professional activities. What is the significance of distinguishing between encountering NOCLAR or suspected NOCLAR and being made aware of it?
- A. The Code recognizes that a PAIB may identify NOCLAR or suspected NOCLAR while carrying out the PA's duties with the employing organization. It also recognizes that another party may bring the matter to the PA's attention, for example, another employee of the organization or an external contractor used by the organization. Section 360 covers both circumstances.
- Q8. Does the Code require PAIBs to detect acts of NOCLAR within the employing organization?
- A. No. The Code does not impose any additional responsibility on PAIBs in this regard beyond the responsibility they already have, if they are in a management role, to ensure that the employing organization's business activities are conducted in accordance with laws and regulations. This management responsibility includes identifying and addressing any instances of NOCLAR.

**Q9.** Is there any expectation under the Code for a PAIB to be able to identify NOCLAR not directly related to the financial statements, for example, in relation to food safety or vehicle emissions requirements?

**A.** There is no expectation under the Code for a PAIB to have a level of understanding of laws and regulations greater than that which is required for the PAIB's role within the employing organization. PAIBs who work in a particular field within the employing organization (for example, corporate taxation or product safety) need an understanding of laws and regulations relevant to that particular field to an extent sufficient to competently carry out their employment duties. In those circumstances, PAIBs are expected to be able to recognize NOCLAR related to the nature of their particular work if information concerning the NOCLAR comes to their attention. However, acts of NOCLAR may be concealed. The Code does not require PAs to search for NOCLAR.

Conversely, the more distant an instance of NOCLAR or suspected NOCLAR (within the scope of Section 360) is from a PAIB's expertise or field of work, the less likely it is that the PAIB will recognize it.

**Q10.** Is a PA expected under the Code to have specialized legal knowledge and skills unrelated to the PAIB's employment responsibilities?

**A.** No. A PA is only expected under the Code to have a level of understanding of laws and regulations necessary for the PAIB to discharge the PAIB's professional duties with the employing organization competently.

#### **Documentation**

**Q11.** Why does Section 360 only encourage documentation for PAIBs and not require it?

**A.** This is consistent with the general approach to documentation in the Code. This approach for PAIBs has been to encourage documentation in their interests and not to require it. In contrast, the Code requires it for auditors in the context of NOCLAR, given their unique role in the public interest and the greater extent of regulatory oversight over them compared with PAIBs.

#### **Effective Date**

**Q12.** The NOCLAR provisions in the Code become effective on July 15, 2017. If a PAIB was already aware of an act or suspected act of NOCLAR prior to that time, is there any obligation under the Code for the PAIB to address it?

**A.** No. The PAIB would need to respond in accordance with Section 360 to any NOCLAR or suspected NOCLAR of which the PAIB becomes aware from July 15, 2017. However, as early adoption is permitted, the provisions may be applied with respect to any NOCLAR or suspected NOCLAR of which the PAIB was aware prior to that date.

**Q13.** The NOCLAR provisions in the Code become effective on July 15, 2017. If an act of NOCLAR had been committed within the employing organization before then and the PAIB only became aware of it on November 15, 2017, is there any obligation under the Code for the PAIB to address it?

- A. Yes. The Code requires a response from the PAIB to any NOCLAR or suspected NOCLAR of which the PAIB becomes aware on or after July 15, 2017. Therefore, in this case, the PAIB would need to respond to the matter in accordance with Section 360.

## II. Senior PAIBs

### Organizational Culture vis-à-vis NOCLAR

- Q14.** Does the Code discuss the role that senior PAIBs can play in promoting a culture of compliance with laws and regulations within their employing organizations?
- A. Yes. Paragraph 300.5 explains that a PAIB is expected to encourage and promote an ethics-based culture in the employing organization, taking into account the PAIB's position and seniority in the organization, and to the extent that the PAIB is able to do so. In the context of NOCLAR, action that the PAIB may take includes the introduction, implementation and oversight of policies and procedures to prevent NOCLAR. Paragraph 300.5 also explains that the more senior the PAIB's position within the organization, the more the PAIB will be able to influence policies, decisions made and actions taken by others involved with the organization.

### Obtaining an Understanding of the Matter

- Q15.** If a senior PAIB becomes aware of NOCLAR or suspected NOCLAR committed by the employing organization in circumstances other than through carrying out the PAIB's employment duties (for example, by coming across the matter on the internet or hearing about it at the PAIB's sports club), is the senior PAIB required to discuss the matter with management or those charged with governance (TCWG)?
- A. Paragraph 360.14 of the Code requires the senior PAIB to obtain an understanding of the matter regardless of the source of the information or how the PA became aware of it. This understanding includes an understanding of the nature of the matter and its potential consequences. If based on this understanding, the PAIB suspects an instance of NOCLAR, Section 360 requires the PAIB to discuss the matter with the PAIB's immediate superior, if any, in order to determine how to address it. If the PAIB's immediate superior may be implicated, paragraph 360.16 requires the PAIB to discuss the matter with a more senior person who is not implicated. This discussion is subject to any internal protocols and procedures regarding how information concerning identified or suspected NOCLAR is to be raised internally. Section 360 also requires the PAIB to bring the matter to the attention of TCWG in order to agree an appropriate response and to enable them to fulfill their own responsibilities.
- Q16.** A senior PAIB becomes aware of suspected NOCLAR committed within the employing organization. The PAIB's immediate superior, however, disagrees with the PAIB regarding the evidence concerning the matter. Does this mean that the PAIB need not pursue the matter further under the Code?
- A. No. The fact that the immediate superior disagrees with the PAIB regarding the evidence concerning the matter is not sufficient grounds for the PAIB to automatically stop pursuing the matter. The PAIB needs to be satisfied that the superior's explanations adequately dispel the PAIB's suspicion. If they do not, the PAIB may consider other courses of action, which will depend on the complexity of the matter and extent of judgment involved. These courses of action include,

for example, consulting with others within the organization, obtaining legal advice, or consulting on a confidential basis with a regulator or professional body. Section 360 also requires the PAIB to escalate the matter to TCWG; to assess the appropriateness of the response of the PAIB's superiors and TCWG; and in the light of the appropriateness of that response, to determine if further action is needed in the public interest.

### Addressing the Matter

- Q17.** If a senior PAIB's superiors and TCWG are unwilling to address the identified or suspected NOCLAR, does this mean that the PAIB has no further responsibilities with respect to the matter under the Code?
- A.** No. Part of the response framework under Section 360 involves the senior PAIB assessing the appropriateness of the response of the PAIB's superiors, if any, and TCWG to the matter. If the PAIB's superiors and TCWG do not address the matter, this would be grounds for the PAIB to conclude that their response is not appropriate. In those circumstances, Paragraph 360.21 requires the PAIB to determine if further action is needed in the public interest. Paragraph 360.22 sets out various factors for the PAIB to consider in making this determination, including the nature and extent of any such further action.

### Disclosure of NOCLAR to an Appropriate Authority

- Q18.** Does the Code require disclosure of NOCLAR or suspected NOCLAR to an appropriate authority if a senior PAIB's superiors, if any, and TCWG have not appropriately addressed the matter?
- A.** No. The Code does not require disclosure. It, however, sets out factors for a senior PAIB to consider in deciding whether disclosure of the matter to an appropriate authority would be an appropriate course of further action. This decision will depend on an objective assessment of the facts and circumstances at the time, taking into account the factors set out in paragraphs 360.22 and 360.29 of the Code, and applying the reasonable and informed third party test in paragraph 360.24. The reasonable and informed third party test is intended to bring an essential element of objectivity to the PAIB's determination of the need for, and nature and extent of, further action. The PAIB is expected to be impartial when assessing the facts and circumstances at the time.
- Q19.** Is there an expectation under the Code for a senior PAIB to disclose *any* identified NOCLAR to an appropriate authority if PAIB's superior(s), if any, and TCWG do not appropriately address the matter?
- A.** No. The provisions in the Code that address disclosure to an appropriate authority (paragraphs 360.28-30) only apply to instances of NOCLAR or suspected NOCLAR where there is credible evidence of actual or potential *substantial harm* to the entity or its stakeholders, including the general public (paragraph 360.22). In other words, such disclosure only becomes a consideration in cases that the PAIB determines, based on the particular facts and circumstances at the time and applying appropriate professional judgment, are "serious."
- Q20.** A clause in a senior PAIB's employment contract requires the PAIB to maintain the confidentiality of the employing organization's information at all times. Does this mean that the PAIB would be precluded from making disclosure of NOCLAR to an appropriate authority under Section 360 if the

PAIB determines that such disclosure would be an appropriate course of action in the circumstances?

- A. No. It is a prerequisite to PAIBs performing professional activities as PAs that they are able to fully comply with the Code, including the provisions in Section 360, unless compliance with a specific provision of the Code is prohibited by law or regulation. To minimize any potential misunderstanding, the PAIB may clarify the PAIB's overriding responsibility to comply with the Code in the employment contract.

**Q21.** Can a senior PAIB resign from the employing organization as a result of identified or suspected NOCLAR without disclosing the matter to an appropriate authority?

- A. Yes. Under paragraph 360.25 of the Code, resignation from the employing organization and disclosure of the matter to an appropriate authority are courses of further action that can be taken independently of each other. In some circumstances, the PAIB might determine that both actions are necessary, although resignation from the organization is clearly not an action to be taken lightly. In this regard, paragraph 360.26 explains that resigning from the employing organization is not a substitute for taking other actions that may be needed to achieve the PAIB's objectives under Section 360.

**Q22.** Paragraph 360.31 explains that in exceptional circumstances where a senior PAIB has reason to believe an imminent breach of a law or regulation would cause substantial harm to investors, creditors, employees or the general public, the PAIB may immediately disclose the matter to an appropriate authority. Does the PAIB need to follow the response process set out in Section 360 to the end before deciding to make such disclosure?

- A. No, the senior PAIB need not go through the whole response process in these circumstances. However, paragraph 360.30 requires the senior PAIB to act in good faith.

### III. **Other PAIBs**

**Q23.** Why are the NOCLAR provisions in the Code applicable to "senior PAIBs" different from those applicable to other PAIBs?

- A. The provisions applicable to senior PAIBs are more demanding because of their higher positions of authority within the employing organization, their greater spheres of influence and decision-making ability, and the greater public expectations of them by virtue of their positions.

**Q24.** A PAIB who is not a senior PAIB as described in Section 360 of the Code becomes aware of information suggesting that an act of NOCLAR might have been committed by the employing organization. What is the PAIB required to do under the Code in these circumstances?

- A. Paragraph 360.33 of the Code requires the PAIB to first seek to obtain an understanding of the matter. If based on that understanding, the PAIB identifies or suspects that the NOCLAR has occurred, paragraph 360.35 requires the PAIB to either raise the matter through the organization's internal protocols and procedures addressing NOCLAR, or escalate it to the PAIB's immediate superior.

- Q25.** A PAIB who is not a senior PAIB as described in Section 360 of the Code suspects that the employing organization has committed an act of NOCLAR. If the PAIB is unable to substantiate the suspicion, does this mean that the PAIB has not complied with the Code?
- A.** No. The Code recognizes that for PAIBs who are not senior PAIBs, there may be limitations on access to information. The PAIB will have fulfilled the PAIB's responsibilities under the Code if the PAIB has made an attempt at obtaining relevant information to substantiate the suspicion.



## Key Contacts

James Gunn, Managing Director, Professional Standards ([jamesgunn@ProfStds.org](mailto:jamesgunn@ProfStds.org))

Ken Siong, Technical Director ([kensiong@ethicsboard.org](mailto:kensiong@ethicsboard.org))

## About the IESBA

The [International Ethics Standards Board for Accountants](#) (IESBA) is an independent standard-setting board that develops and issues high-quality ethics standards and other pronouncements for professional accountants worldwide. Through its activities, the IESBA develops the *Code of Ethics for Professional Accountants*, which establishes ethical requirements for professional accountants.

The objective of the IESBA is to serve the public interest by setting high-quality ethics standards for professional accountants and by facilitating the convergence of international and national ethics standards, including auditor independence requirements, through the development of a robust, internationally appropriate code of ethics.

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