Dear Jörgen,

The Professional Accountants in Business (PAIB) Committee of the International Federation of Accountants (IFAC) values the opportunity to comment on the International Ethics Standards Board for Accountants (IESBA)’s Exposure Draft proposing changes to the Code of Ethics for Professional Accountants (the Code) addressing responding to a suspected illegal act. The PAIB Committee seeks to provide the perspective of professional accountants in business, which is further elaborated in Appendix A.

Overall Comments

In this section, the PAIB Committee provides a number of overall comments and recommendations, as well as raises some additional issues that do not fit under IESBA’s request for specific comments.

Clarify the need for the proposed changes

The explanatory memorandum does not truly clarify the need for the proposed changes. Section 140.7 of the current Code already provides the overall provision that the professional accountant “may be required to disclose confidential information [in case of] a professional duty or right to disclosure when not prohibited by law.” Does the IESBA have evidence or strong indications that there are issues with the application of this principle? When preparing the impact analysis, did the IESBA also consider the impact if the proposed changes to the Code are not implemented? Improved clarification of, or further research into the need for, this addition to the Code would be welcome.

Change “requirement” into “apply or be able to explain”

The PAIB Committee is of the view that the proposed changes to the Code are confusing regarding whether disclosing certain illegal acts to an appropriate authority is a right or a requirement. Paragraph 360.1, for example, discusses having a right, whereas paragraph 360.8 uses the prescriptive “shall disclose” construction. Another example is paragraph 360.9 which first states the right to disclose, but then adds that “a professional accountant is expected to exercise this right to disclose in order to fulfill the accountant’s responsibility to act in the public interest.” In practice, an individual would find it hard to identify a significant difference in the Code’s differentiation between “is expected” and being “required” to exercise the “right” to disclose, in particular when the proposed text goes on to state in paragraph 360.10 that only in “exceptional circumstances” would the professional accountant “not be expected” to make the disclosures.
Having a right does not generally impose a demand on those who have it. Placing an expectation on how to exercise a right is not consistent with the concept of having a right.

The IESBA could take a more principles-based approach to disclosure; that is, along the lines of the familiar governance approach of “apply or be able to explain.” That is, professional accountants should apply the principle to ultimately disclose a suspected illegal act or be able to explain, after the fact if necessary, why they did not. This would also fit neatly with the provision in paragraph 360.15 that “the professional accountant shall document the steps the accountant took to respond to suspected illegal acts.”

*Allow for cultural or legal differences*

Taking an “apply or be able to explain” approach to the proposed changes in the Code would also enable greater diversity for culturally sensitive differences, for example, with respect to whistleblowing policies or the reasonable third party test. This would further increase the universal usefulness to professional accountants in business.

An “apply or be able to explain” approach would also bolster professional accountants who work in jurisdictions with weak or no whistleblower and witness protection laws. In addition, in some jurisdictions, reporting illegal acts without sufficient evidence can amount to false or malicious reporting and the penalties are extremely punitive. This distinct possibility is noted in the impact analysis in the appendix to the exposure draft, but appears to not be further addressed. Therefore, in our view, if the questionable concept of being expected to exercise a right to disclose is retained, the notion of potentially severe legal consequences for the professional accountant in business should be included as an additional example in paragraph 360.10.

*Resignation should be last resort*

Paragraph 360.3 requires the professional accountant in business who identifies a suspected illegal act to consider whether it is appropriate, based on all relevant facts and circumstances, to resign from the employing organization. The PAIB Committee is of the opinion that resignation should be the last resort, as the professional accountant in business should first attempt to appropriately address the matter. In addition, the requirement to resign can place an undue burden on professional accountants in business as it effectively means they would be required to give up their personal income.

The requirement to resign could be disproportionate in case of suspected illegal acts, which may be minor offenses. The Code should recognize that suspected illegal acts can have various levels of severity. Professional accountants in business should apply professional judgment, and take account of subsequent steps to be taken, in determining the severity of the act.

Therefore, paragraph 360.3 should clearly state that resignation is the last resort. In addition, the PAIB Committee recommends moving this paragraph closer to the end of Section 360 to emphasize that other actions should come first. In this respect, please also see the last sentence of paragraph 360.10 that says: “if the professional accountant does not exercise this right, the accountant shall consider whether to resign from the employing organization.”

Comments on the specific questions outlined in the Exposure Draft follow. Our responses are intended to be read as applying to professional accountants in business.
We have not responded to questions 4-10 as they refer to matters specific to professional accountants in public practice. Instead, we would like to provide the following more general viewpoint: The PAIB Committee believes a professional accountant in public practice has a moral and professional duty, from a public-interest perspective, to follow up on a suspected illegal act, even when performing non-audit services to a non-audit client. This should take place through the internal governance layers of the client organization until the highest governing body is reached.\(^1\) Ultimately, if all internal options are exhausted and the issue is still not sufficiently resolved, and depending on the type and severity of the suspected illegal act, the professional accountant in public practice has the responsibility and duty, following the same “apply or be able to explain” approach as we recommend for professional accountants in business, to override the fundamental principle of confidentiality and disclose a suspected illegal act to an appropriate external authority.\(^2\)

**Specific Comments**

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

We do not necessarily agree. Paragraph 360.5 states that “if the professional accountant is unable to dispel the suspicion, the accountant shall determine the appropriate course of action, taking into account whether the organization has an established mechanism, such as an ethics policy, for addressing such matters.”

The PAIB Committee believes that following established mechanisms in an organization, when present, such as reporting to a designated compliance officer and beyond (“escalation ladder”), should be the preferred way to resolve a suspicion. Only when these mechanisms do not exist, or do not work properly, should the professional accountant in business follow the procedure proposed in paragraph 360.6 of the Code. In addition, the committee notes that question 1 uses the term “should be required.” Although this term is not used in the proposed changes to the Code, the committee would like to emphasize that it is strongly opposed to a requirement in this area and proposes use of a principles-based “apply or be able to explain” approach instead.

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

We agree. However, as mentioned in our general comments, the PAIB Committee believes that the proposed changes to the Code are confusing regarding whether disclosing certain illegal acts to an appropriate authority is a right or a requirement. We, therefore, recommend the IESBA replace the requirement with a principles-based “apply or be able to explain” approach in these circumstances.

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\(^{1}\) In some organizations the audit committee might be the most appropriate body to address in these circumstances.

\(^{2}\) It might be worth considering having an agreement between the organization that employs the services of an audit firm and the audit firm include a specific clause relating to overriding the principle of confidentiality should the company not respond responsibly and/or appropriately to the auditor reporting a suspected illegal act.
Question 3. Do respondents agree that the threshold for reporting to an appropriate authority should be when the suspected illegal act is of such consequence that disclosure would be in the public interest? If not, why not and what should be the appropriate threshold?

We agree. Being in the public interest is an appropriate threshold for reporting to an appropriate authority. In this respect, the PAIB Committee notes that “the public interest” is wider than “the general public” and can consist of all types of stakeholders.

Contrary to the IESBA, however, the PAIB Committee believes that disclosures of suspected illegal acts within smaller organizations without an external auditor can still be in the public interest. Not only because various external or internal stakeholders, including employees, could be severely disadvantaged by such illegal acts (for example, society as a whole in the case of tax fraud), but also because having a professional accountant in business who is acting inappropriately could damage confidence in the profession.

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

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

We partly agree. As discussed under question 1, the PAIB Committee believes that following established mechanisms in an organization, when present, such as reporting to a designated compliance officer and beyond (to the governing body and possibly to designated external parties), should be the preferred method of reporting. Only when these mechanisms do not exist, or do not work properly, disclosure to the entity’s external auditor may be appropriate.

The consequences of using the concept of “informing the external auditor” should be further clarified in the guidance. Questions that may remain for some users include: What would happen next? What is the cost versus benefit? How should the identity of any internal whistleblower be protected? How does this apply to entities without an external auditor?

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

We partly agree. As discussed in the general comments, the PAIB Committee believes that the right to override confidentiality and disclose is already included in Section 140 of the current Code. In addition, and as discussed above, the committee proposes an “apply or be able to explain” approach rather than the proposed requirement in paragraph 360.9 of the Code. As indicated above, placing an expectation on how to exercise a right is not consistent with the concept of having a right. Therefore, our view is that

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3 See the IESBA’s Explanatory Memorandum under “Entities with No External Auditor.”
4 Based on the professional accountant in business’ professional judgment, taking into account, for example, the level of legal protection in case of such a disclosure.
5 This is especially important if the whistleblower is a professional accountant in business acting in accordance with another part of the Code.
professional accountants should not be required or expected to exercise the right but, instead, may be
required or expected to exercise their judgment whether or not to disclose in accordance with the “apply or
be able to explain” principle.

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

We partly agree. With regard to the first bullet point of paragraph 360.9 (acts that affect financial reporting),
it should be noted that financial reporting is not necessarily related to a professional accountant in
business’ specific expertise and responsibilities within his or her organization. The second bullet point only
partly repeats the general formulation as used on page 8 of the explanatory memorandum that says: “the
IESBA is of the view that such acts are those that are related to the expertise and responsibilities of the
professional accountant in his or her particular role.” The committee recommends the IESBA replace both
bullet points with this more general formulation.

*Other*

**Question 14.** Do respondents agree that in exceptional circumstances a professional accountant
should not be required, or expected to exercise the right, to disclose certain illegal acts to an
appropriate authority? If not, why not and what action should be taken?

We partly agree. As discussed above, the PAIB Committee is of the view that the professional accountant
should not be required or expected to exercise the right but, instead, should be required or expected to
exercise his or her judgment whether or not to disclose in accordance with the “apply or be able to explain”
principle.

**Question 15.** If respondents agree that in exceptional circumstances a professional accountant
should not be required, or expected to exercise the right, to disclose certain illegal acts to an
appropriate authority, are the exceptional circumstances as described in the proposal appropriate?
If not, how should the exceptional circumstances be described?

We partly agree. The PAIB Committee believes that these circumstances are appropriate as examples but
that professional accountants, through their professional judgment, should be able to determine for
themselves what circumstances are exceptional, including, as mentioned above, retaliation or intimidation
through the law (e.g., libel laws) or other forms of retaliation or intimidation in addition to physical threats or
weak regulatory frameworks.

In addition, the exceptional circumstances that may remove the expectation to disclose to an external
authority seem to be based on the assumption that professional accountants will be able to assess all
threats or forms of retaliation prior to them making any disclosure. The experiences of many whistleblowers
do not support this view, regardless of whether there is an organizational policy or a law against retaliation.
Question 16. Do respondents agree with the documentation requirements? If not, why not and what documentation should be required?

We agree. See our general comments regarding changing “requirement” into “apply or be able to explain.” However, the PAIB Committee is concerned over the proper security of such documentation, especially if it is determined that no illegal act took place and disclosure is not necessary. Some guidance on proper safeguarding of the documentation based on its sensitivity should be included in any changes to the Code.

Question 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?

No comments.

Question 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 partly agree. As discussed in the general comments, the PAIB Committee believes additional analysis on the future impact if the proposed changes to the Code are not implemented could further clarify the need for this additional guidance. In addition, the impact analysis could be expanded to also include professional accountants who sit in governance bodies, such as boards and policy-setting bodies.

Please do not hesitate to contact me should you wish to discuss any of the matters raised in this submission. We also welcome further discussions on how the PAIB Committee can continue supporting the work of the IESBA.

Kind regards,

Roger Tabor
Chair, IFAC Professional Accountants in Business Committee
Appendix A: Perspective of the Professional Accountant in Business

The following two PAIB Committee publications further illustrate the perspective of professional accountants in business.

*Competent and Versatile: How Professional Accountants in Business Drive Sustainable Organizational Success* (2011) establishes the expectations placed on professional accountants in business in terms of the roles and activities they will need to undertake, thereby extending beyond the traditional knowledge and skills that will be taught and tested during their professional education. It also emphasizes that professional accountants in business should uphold high ethical standards in accordance with the Code, which requires accountants to encourage an ethics-based culture in any employing organization.

*Defining and Developing an Effective Code of Conduct for Organizations* (2007) highlights the important role that professional accountants in business can play in driving and supporting organizational ethics and fostering a values-based organization. By applying a values-based approach and leading by example rather than relying only on written policies and rules, professional accountants in business can promote a culture that encourages employees to internalize the principles of integrity by allowing them to make appropriate decisions given specific circumstances.

More information about the PAIB Committee and its publications is available at [www.ifac.org/paib](http://www.ifac.org/paib).