

September 3, 2015

Chair
International Ethics Standards Board for Accountants
545 Fifth Avenue, 14th Floor
New York, New York 10017

Re: *Exposure Draft, Responding to Non-Compliance with Laws and Regulations*

Dear Members of the International Ethics Standards Board for Accountants:

We appreciate the opportunity to provide comments on the exposure draft “*Responding to Non-Compliance with Laws and Regulations*” (the “Exposure Draft”) issued May 2015 by the International Ethics Standards Board for Accountants (“IESBA” or “Board”).

General Comments

We are supportive of IESBA’s objective to serve the public interest by setting high-quality ethical standards for professional accountants (“PAs”). It is important that the Board not only set these ethical standards, but provide useful, actionable guidance for PAs in order to help them understand and meet their responsibility to act in the public interest. Overall, we believe the Board has put forth a proposal that balances the expectations for the various categories of PAs with the responsibilities of management and those charged with governance (“TCWG”) or the employing organization, as applicable, when the PA suspects or observes instances of non-compliance with laws and regulations (“NOCLAR”). We are especially supportive of the Board’s efforts to align proposed section 225 with the existing requirements of ISA 250, *Consideration of Laws and Regulations in an Audit of Financial Statements* (“ISA 250”) as consistency between the Code and ISAs should be sought wherever possible.

The proposals should be successful in raising the PA’s awareness of the need to have an understanding of requirements that may exist in particular jurisdictions that govern how professional accountants should address an instance of identified or suspected NOCLAR. This increased awareness may improve understanding of existing requirements which helps to serve the public interest. The more difficult objective of the proposed standard is to provide globally applicable guidance to PAs to help guide their actions in cases where there are no legal or regulatory requirements that provide what they must do to respond to identified or suspected NOCLAR. We consider this objective is met as whole, subject to the comments below.

In separating the guidance for PAs in public practice between auditors and non-auditors, IESBA has appropriately recognized the auditor’s higher obligation to act in the public interest when acting in that capacity and coming across identified or suspected NOCLAR at

the entity being auditing. We agree that a PA providing non-audit services should not be able to turn a blind eye if he/she comes across identified or suspected NOCLAR during the performance of a non-audit engagement, especially if there is a potential for substantial harm to the public. However, it is not clear how the non-auditor will necessarily have the ability to discharge all of his or her obligations under the proposal. In particular, when requiring the PA to consider whether further action is needed, logically the PA would need to consider the appropriateness and timeliness of management's response to the NOCLAR. While an auditor typically has the ability to force conversations with the appropriate levels of management to understand how a matter is being addressed, especially if there is potential for the identified or suspected NOCLAR to have a material effect on the financial statements, a non-auditor typically does not have the same leverage. The proposal assumes the non-auditor will have a continuing role in addressing the matter with the client, but management has no obligation to discuss its actions with the non-auditor and the non-audit engagement may have been completed long before management responds. Management may in fact be acting appropriately, but the non-auditor may not have the ability to obtain the information necessary to determine whether further action is needed. In such a case, what would the non-auditor be expected to do under the proposed standard? We consider that the non-auditor's responsibility under the proposal should end with reporting the matter to the appropriate level of management. Alternatively, the proposal should make it clear that the professional accountant may not be able to access the information necessary to be able to determine whether further action is needed.

We also have concerns about the requirement for the non-auditor to report the identified or suspected NOCLAR to the audit partner when the client is an audit client of that firm. Such reporting may not be permitted under law in certain jurisdictions. This may lead to a conflict between the Code and local law, which is especially problematic in those jurisdictions where the Code is adopted into law. The Board should consider the following amendment to paragraph 225.39: "If the professional accountant is performing a non-audit service for an audit client of the firm, the professional accountant shall communicate the matter within the firm unless such communication is prohibited under law or regulation."

Finally, the proposal does not adequately address instances where there may be a difference in professional judgement about whether the matter is in fact non-compliance with laws and regulations. While the Exposure Draft does state whether an act constitutes actual non-compliance is ultimately a matter for determination by an appropriate legal or adjudicative body, the proposal does not consider the likelihood of the matter being actual non-compliance when determining if further action should be taken. Tax law is an example where there may be a wide variation in interpretation and only the tax authorities would make the ultimate determination of whether a particular tax treatment is permissible. Identified tax fraud, on the other hand, would not have this same level of uncertainty. We suggest the following to be added to the list of factors to be considered by all PAs when determining if further action needs to be taken: "The degree of professional judgement in determining if the matter is an instance of non-compliance with laws and regulations."

Our comments to the questions raised in the Exposure Draft are provided below.

Specific Comments

- 1. Where law or regulation requires the reporting of identified or suspected NOCLAR to an appropriate authority, do respondents believe the guidance in the proposals would support the implementation and application of the legal or regulatory requirement?**

If there is a law or regulation that requires the reporting of identified or suspected NOCLAR to an appropriate authority, it is our presumption that a PA will abide by the requirements in the particular jurisdiction. The inclusion of provisions in the Code that requires a PA to abide by such laws and regulations will help to reinforce the need for a PA to gain an understanding of the requirements in their local jurisdiction if they are not already doing so. As such, we believe the proposals will support the implementation and application of these requirements.

- 2. Where there is no legal or regulatory requirement to report identified or suspected NOCLAR to an appropriate authority, do respondents believe the proposals would be helpful in guiding PAs in fulfilling their responsibility to act in the public interest in the circumstances?**

We believe the proposals will help PAs understand and fulfill their responsibility to act in the public interest, but the provisions are predicated on the assumption that the PA has the necessary information to make certain judgements and determine whether further action is needed. The proposals do not address the situation or provide guidance on what can be done if, despite best efforts, the PA does not have sufficient information to be able to determine whether further action is needed and meet the objectives of the proposal. There are also other areas where additional guidance would be useful to lead to a consistent application of the standard and these matters are more fully described below.

- 3. The Board invites comments from preparers (including TCWG), users of financial statements (including regulators and investors) and other respondents on the practical aspects of the proposals, particularly their impact on the relationships between:**

- a. Auditors and audited entities;**

As proposed, Section 225 strikes an effective balance describing the responsibilities for the auditor and management/TCWG. We agree with placing a greater emphasis on the responsibility of management with the oversight of TCWG to ensure that the client's business activities are conducted in accordance with laws and regulations, while recognizing that the auditor has a responsibility to alert management/TCWG when the auditor becomes aware of identified or suspected NOCLAR, so that proper action may be taken. We believe that it will be extremely rare that an auditor will be driven to the point of needing to disclose NOCLAR to an appropriate authority (unless required to do so in terms of applicable law or regulation). The more balanced approach in the revised proposal guides the auditor through the actions the auditor should take in the context of performing an audit of the entity's financial statements, including the ultimate documentation of the matter. Because reporting to authorities is expected to be rare, we do

not believe the ability to do so should constrain the flow of information from management and those charged with governance to the auditor. This free flow of information is key to enabling the auditor to discharge his or her responsibilities when performing the audit and for maintaining audit quality.

b. Other PAs in public practice and their clients; and

The revised proposal recognizes the importance of other PAs in public practice serving as advisers to their clients and not acting as “watchdogs”. The different level of requirements in the proposal for other PAs in public practice also recognizes the different degree of access to management/TCWG such PAs may have as compared to auditors. We are especially supportive that the proposal states other PAs in public practice may take into consideration whether reporting the identified or suspected NOCLAR to third party would be contrary to law or regulation or whether the terms or nature of the engagement preclude such disclosure. There are other aspects of the proposal, however, that may be difficult for a non-auditor to fulfill. The proposal provides guidance for the non-auditor when there is no applicable law or regulation governing how the non-auditor PA would be required to address identified or suspected NOCLAR. In order to follow this guidance, the PA would need to have access to management in order to obtain a detailed understanding of the matter and the related actions that are being undertaken. If the PA suspects or has identified an instance of NOCLAR, we presume that management would welcome information by the PA so that management can take action to address the matter. However, subsequent to the initial communication, management may not wish to continue to involve the PA in the matter and would be under no regulatory or legal obligation to do so. This situation could potentially put the non-auditor in a difficult position when attempting to fulfill his or her obligations as proposed by the revisions to the Code. We recommend the addition of the following consideration in the list presented in paragraph 225.42: “Whether the professional accountant has the information necessary to make the appropriate judgement.”

c. PAIBs and their employing organizations.

We feel the proposals appropriately delineate what would be expected for a senior PAIB and other PAIBs and are well balanced in assigning responsibilities for the employing organization and the PAIBs. However, resigning from an employing organization is an option for other PAIBs just as much as senior PAIBs, but this option is only presented for senior PAIBs in the proposal. We suggest adding this as a potential course of action for other PAIBs who no longer wish to be associated with the employing organization. This is also consistent with Section 100.24 where disassociation is required in the case of ethical conflicts.

Specific Matters

4. Do respondents agree with the proposed objectives for all categories of PAs?

We agree that the first two proposed objectives (to enable PAs to comply with the fundamental principles of integrity and professional behavior, and to alert management or

where appropriate, TCWG to enable action to be taken to address identified or suspected NOCLAR or deter commission of NOCLAR) are appropriate for all categories of PAs. We believe the third objective (for PAs to take such further action as may be needed in the public interest) may be difficult for certain categories of PA, especially PAs in public practice providing non-audit services and PAs in business other than senior PAs. Meeting this objective may not be possible in the circumstances, especially if the individual PA (despite best efforts) does not have the necessary information to determine the next action to take or is precluded by law or regulation from taking further action. We suggest editing the third objective as follows: “(c) Where possible, to take such further action as may be needed in the public interest.”

5. Do respondents agree with the scope of laws and regulations covered by the proposed Sections 225 and 360?

We agree with the scope of laws and regulations covered by the proposed section 225 and are especially supportive of the Board’s efforts to align the proposal with ISA 250 *Consideration of Laws and Regulations in an Audit of Financial Statements*. We are also supportive of the Board’s decision to scope out matters that are “clearly inconsequential”. We believe however that adding some of the examples that are included in the background information of the proposal into the two proposed sections will lead to a more consistent application of the standard.

6. Do respondents agree with the differential approach among the four categories of PAs regarding responding to identified or suspected NOCLAR?

We agree with the differential approach for the four categories of PAs. We agree that auditors and senior PAIBs should be held to a higher standard based on the greater public interest expectations of those roles as well as the greater access PAs in those roles have to the highest levels of management and TCWG. While non-auditors and junior PAIBs may not be subject to the same expectations or may have more limited access to information or more senior levels of management/TCWG, we agree that PA’s serving in these roles cannot just turn a blind eye to identified or suspected NOCLAR, especially if it would result in substantial harm to others. The proposals provide appropriate guidance for those categories of PAs, assuming they have continued involvement with management and can obtain necessary information about the matter to make informed decisions.

7. With respect to auditors and senior PAIBs:

a. Do respondents agree with the factors to consider in determining the need for, and the nature and extent of, further action, including the threshold of credible evidence of substantial harm as one of those factors?

The factors are quite expansive and we believe most of the factors in the list should be useful in determining the nature and extent of further action. There may be difficulty in practice, however, in determining what is meant by “substantial harm” and in applying the threshold to particular facts and circumstances. We believe it would be useful for the Board to consider providing additional guidance in that area to ensure a consistent application of the standard.

b. Do respondents agree with the imposition of the third party test relative to the determination of the need for, and nature and extent of, further action?

We agree with the inclusion of the third party test as proposed.

c. Do respondents agree with the examples of possible courses of further action? Are there other possible courses of further action respondents believe should be specified?

We agree with the examples given for possible courses of further action. We recommend the following edit to paragraphs 225.24 and 360.23 to increase the readability of the standard, especially for non-native English speakers: “Disclosing the matter to an appropriate authority ~~notwithstanding that~~ even when there is no legal or regulatory requirement to do so.”

d. Do respondents support the list of factors to consider in determining whether to disclose the matter to an appropriate authority?

We are supportive of all of the factors that are included in the proposals, but further edits would be useful to add clarity to this section.

- The following edit to paragraphs 225.27 and 360.26 will increase the readability of this statement: “Products that are harmful to public health or safety and would be likely ~~to be~~ sold by the entity.”
- While the concept of “tipping-off” has been addressed in paragraph 225.10, it should be included again in paragraph 225.29 through the following edit: “The professional accountant shall also consider whether it is appropriate to inform the client of the professional accountant’s intentions before disclosing the matter when doing so is not prohibited by law.”

8. For PAs in public practice providing services other than audits, do respondents agree with the proposed level of obligation with respect to communicating the matter to a network firm where the client is also an audit client of the network firm?

The reporting of non-compliance with laws and regulations to the audit partner can help to increase audit quality by enhancing the audit partner’s understanding of the entity and its environment in order to identify and assess the risks of material misstatement of the financial statements. We are supportive of the proposal that the non-auditor PA is required to consider whether identified or suspected NOCLAR should be communicated to a network firm when the client is also an audit client of the network firm, but such communication is not mandated. The proposed consideration as to whether to communicate provides the necessary flexibility in the event that communicating across different firms within a network may be contrary to law or regulation in certain jurisdictions. As mentioned previously, we also urge the Board to consider whether the requirement for a non-auditor PA to report such matters within the same firm is appropriate given such reporting may be precluded under local laws or regulations. We feel it would be appropriate to include a statement in paragraph 225.39 that reporting within the firm by the non-auditor PA is only required if not contrary to local laws or regulations.

9. Do respondents agree with the approach to documentation with respect to the four categories of PAs?

Yes, the approach to documentation is appropriate for the various categories of PAs.

Other general comments:

We would like to make the following comments that do not fall within the specific questions asked:

- Another potential avenue for a PA in professional practice to report an observed or suspected NOCLAR is the client’s internal ethics reporting guidelines, such as through the Chief Ethics Officer. The Board may wish to consider adding this concept to paragraph 225.16 just as it has been pointed out in paragraph 360.11.
- We are unclear how a client that is other than management, an employee or TCWG would commit a NOCLAR as those three groups would seem to encompass all individuals who would comprise the “client”. Therefore, we suggest the following edit to paragraph 225.2: “Non-compliance with laws and regulations comprises acts of omission or commission, intentional or unintentional, committed ~~by a client, or by management,~~ those charged with governance, ~~management~~ or employees of a client which are contrary to the prevailing laws or regulations.”
- Paragraph 225.19 addresses the timing of reporting by stating “some laws and regulations may stipulate a period within which reports are to be made” but this is not addressed in any other part of the proposal. The relevance of this point is therefore not clear.
- Paragraph 100.26 is proposed to be added to the extant Code, but neither the relationship between that addition and the NOCLAR proposed standards, nor the need for this new paragraph are clear.

Drafting comments:

We suggest the following edits to enhance the readability of the proposed standards:

- Include a general comment in the beginning of sections 225 and 360 to specifying the types of professional accountants (i.e., professional accountants in professional practice, professional accountants in business) to whom the section applies.
- 225.30: Where the professional accountant determines that withdrawing from the engagement and the professional relationship would be appropriate and such a

withdrawal is permissible under law or regulation, doing so would not be a substitute for taking other actions that may be needed to achieve the professional accountant's objectives under this section. In some jurisdictions, however, there may be limitations as to the further actions available to the professional accountant and withdrawal may be the only available course of action.

- 225.37: “Whether an act constitutes actual non-compliance with a law or regulation is ultimately a matter for determination by an appropriate legal or adjudicative body.”
- 225.41: The professional accountant shall ~~also~~ consider whether further action is needed to achieve the professional accountant's objectives under this section.”

* * *

We would be pleased to discuss our comments with members of the IESBA or its staff. If you wish to do so, please feel free to contact Wally Gregory, Managing Director Global Independence, via email (wgregory@deloitte.com) or at +1 203 761 3190.

Sincerely,

A handwritten signature in cursive script that reads "Deloitte Touche Tohmatsu Limited".

Deloitte Touche Tohmatsu Limited