14 December 2012

Comments from FSR, Denmark, on IESBA Exposure Draft: “Responding to a Suspected Illegal Act”

The Ethics Committee of “FSR – danske revisorer” has discussed the IESBA Exposure Draft (ED) from August 2012.

We are pleased to submit the following comments. Because we would not support such an amendment to the Code of Ethics we did not find it necessary to answer each specific question in the ED.

We fully concur in the ideas that all relevant parties should fight against violations of law and regulations in the corporate world. However, we do not find it appropriate and workable to put the measures indicated in this ED into the Code of Ethics for Professional Accountants. Such measures belong to legislation.

We participate in the Ethics Working Party of Federation des Experts Comptables Europeens (FEE) and therefore we have followed the preparation of the draft comment letter from FEE, which we support. Like FEE we do not support the overall and detailed proposals in the ED.

The ED would introduce a broad range of requirements to be applied by professional accountants in public practice as well as in business. We do not find that these requirements (burdens) to be imposed to public accountants would be proportionate with the potentially effect (benefits).

In any event, we find it would not be appropriate introducing specific requirements only for professional accountants (members of IFAC bodies) and not for other professionals since this would not ensure a level playing field for professionals. A negative consequence would be that clients or other people would be more cautious when communicating with professional accountants – contrary to other professionals - and maybe they would be encouraged to acquire professional services from other professionals, thereby not being sure to acquire the best possible service for that particular assignment. We refer to the joint international efforts to set up measures against money laundering and financing of terrorism. Those measures are dealing with different kind of professionals – including also lawyers, bankers etc. – and regardless of whether they are members of their relevant professional bodies or non-members. Also consultancy firms operating in the same professional areas as professional accountancy firms should be covered. Moreover, the issue of cross-border engagements would be much
better handled through a similar (harmonized) regulation across borders and this would only be ensured through such international efforts to promote national regulation and enforcement.

We agree, of course, that a suspected fraud or other illegal act must be addressed and that preventive measures should be developed and provided.

Suspected fraud or other illegal activity should be addressed by the management and those charged with governance of the company.

Also the statutory auditors should play a role, which they already do in many countries – e.g. in Denmark.

Such measures should be addressed by legislation, and such legislation should be promoted by international institutions like G20, IOSCO and the European Commission besides national authorities in the same way as protective measures against money laundering and financing of terrorism. In contrast to such measures, the Code of Ethics is not a legal instrument. Therefore, the Code of Ethics can not provide protection e.g. against lawsuits from clients, which might be injured by the auditor’s reporting of seccreces to the authorities. Such protection should be in place, especially because the reporting is not only dealing with ascertainable facts, but (also) regarding suspicion of illegal acts.

We find that the proposals in the ED are confusing and therefore we fear that they will not be workable in practice unless further guidance is provided.

We have noticed that a professional accountant is not required to comply with a particular part of the Code of Ethics if there is a conflict with an existing law or regulation, cf. section 100.1 of the Code, and we have specifically noticed that national legislation overrule the Code in matters of responding to a suspected illegal act, cf. section 225.2 and 360.2 in the ED. However, there will still be a lot of confusion regarding when to fulfill or not specific requirements in this part of the Code of Ethics and there will be several practical difficulties arising from the proposals.

One example is the scope of suspected illegal acts to be reported. We find that the wording “suspected illegal act” is very broad, and so would be the disclosure requirement, unless a clarification is elaborated on section 225.11 (regarding “in the public interest”) and on section 225.13 (regarding “directly or indirectly affect the client’s financial reporting”).

Another example is the threshold of materiality, since we believe that very small and trivial illegal acts should not be reported to an authority as they are of no relevance to the public interest.

Furthermore, according to current Danish legislation the auditor only has to respond, if the auditor “realizes” the crime (which we believe is a higher level of probability than “suspects”) and has reason to assume that the crime concerns significant sums or is otherwise of a serious nature. Such clarifications on the scope are missing in the ED.

**Legislation already in place in Denmark**

For your information the Danish Act on Approved Auditors and Audit Firms – Act No. 468 of 17 June 2008 – already requires (section 22):
Reporting on Financial Crime

S. 22. If the auditor realizes during the performance of assignments in pursuance of Section 1 (2) and (3)1 that one or more members of the company’s management commit or have committed financial crimes in connection with the performance of their managerial duties, and if the auditor has reason to assume that the crime concerns significant sums or is otherwise of a serious nature, the auditor shall immediately notify each individual member of the management hereof. The notification shall be entered in the auditors’ records if the auditor keeps such records. If the management has not documented to the auditor within 14 days at the latest that it has taken the necessary steps to stop any ongoing crime and to remedy the damage that the alleged crime has caused, the auditor shall immediately notify the Public Prosecutor for Serious Economic Crime about the assumed crimes. Sentence 1 and 3 shall not apply to circumstances that are covered by the rules in the Danish Act on Preventive Measures against Money Laundering and Financing of Terrorism.

(2) If the auditor finds that notification of the members of the management will not be a suitable measure for the prevention of continued crime, the auditor shall immediately notify the Public Prosecutor for Serious Economic Crime of the assumed financial crimes. The same shall apply if the majority of the company’s members of the management are involved in or have knowledge of the financial crimes.

(3) If the auditor resigns from his or her position, cf. Section 18 (2), and this is a result of the auditor having reason to assume that there is a situation as described in (1), first sentence, the auditor shall immediately notify the Public Prosecutor for Serious Economic Crime hereof and of the reasons for the auditor’s resignation from his or her position.

Also the Danish Act on Preventive Measures against Money Laundering and Financing of Terrorism and the rules on the auditors report on financial statements stipulate obligations to report on financial crime.

Furthermore, the act defines the duty of professional secrecy – by reference to the Danish Criminal Code. However, the professional secrecy is overruled in those situations, where the auditor is not required to report in his/her auditor’s opinion, in the auditor’s long-form report or directly to members of the management or the Public Prosecutor for Serious Economic Crime.

If you need some clarification of our comments, please do not hesitate to contact us.

Yours sincerely

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Chairman of the
Ethics Committee of
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1 I.e. if the professional accountant shall perform audit or express a professional opinion during performance of the assignment..