

EXPLORING THE IESBA CODE

Installment 9: Responding to Non-Compliance with Laws and Regulations [for PAPPs]



A distinguishing mark of the accountancy profession is its acceptance of responsibility to act in the public interest. Professional accountants might come across situations where they determine, or suspect, that their employing organization or a client is not compliant with laws or regulations. The Code's fundamental principles of integrity and professional behavior require accountants to respond to non-compliance with laws and regulations (NOCLAR) by taking appropriate action, putting the interests of the public first.

When a **PAPP** becomes aware of, or suspects, that NOCLAR has occurred or might occur, the PAPP is required to alert management or, where appropriate, those charged with governance.

- The objective is to enable the client to rectify, remediate, or mitigate the consequences of the identified or suspected non-compliance (or deter the commission of the non-compliance if it has not yet occurred).
- The PAPP is also required to take further action as appropriate in the public interest.

Examples of relevant laws and regulations include those that deal with:

- Fraud, corruption, and bribery
- Banking and other financial products/services
- Data protection
- Tax and pension liabilities/payments
- Environmental protection
- Securities markets and trading
- Money laundering, terrorist financing and proceeds of crime
- Public health and safety

Some laws and regulations (such as financial reporting or tax laws) might have a direct effect on the client's financial statements. In other situations, the laws or regulations might not impact financial statements, but compliance might be critical to the operating aspects of the client's business, to its ability to continue its business, or avoid material penalties (such as environmental regulations).

Greater Obligations for Auditors

Because of the nature of audit and review engagements and the public's expectations of such engagements, PAPPs providing such engagements have higher obligations than PAPPs engaged in work other than audits and reviews.

Auditors must also comply with [ISA 250](#), which addresses audit-specific requirements for considering laws and regulations.

What about confidentiality?

- Disclosure of NOCLAR to an appropriate authority will not be considered a breach of the duty of confidentiality.
- The PA must act in good faith and exercise caution when making statements and assertions, and consider whether to inform the client.

CONSIDER THE FOLLOWING SCENARIO: A technology company has developed and patented a very promising facial recognition system. The product line responsible for the system has run into difficulty as the emerging awareness of bias in its AI algorithms has slowed sales. In desperation, the product manager—the CEO’s protegee—has engaged with an outside vendor in a cryptocurrency money-laundering scheme, the proceeds of which are designed to temporarily mask the division’s falling cashflow until the algorithms can be fixed.

THE PAPP TAKES ACTION DEPENDING ON THEIR ROLE PAPP ON AN AUDIT ENGAGEMENT:

If the auditor identifies or suspects NOCLAR after discovering an unusual series of transactions involving cryptocurrency exchanges known to be at higher risk for money laundering, they would need to:

- Obtain an understanding of the matter, including the nature, circumstances, how laws and regulations apply, and the consequences for the client and stakeholders.
- Discuss the matter with the appropriate level of management or, if senior management is determined to be involved in wrongdoing, discuss it with those charged with governance (such as the audit committee).
- Advise management or those charged with governance to:
 - Rectify, remediate, or mitigate the consequences of any non-compliance;
 - Prevent non-compliance if it hasn’t yet occurred;
 - Disclose the matter to an appropriate authority where required by law or regulation or where necessary in the public interest.
- Consider whether management and those charged with governance understand their legal or regulatory responsibilities in the matter.
- Comply with laws, regulations and auditing standards (such as ISA 250).

The auditor would also be expected to:

- Assess the appropriateness of the client’s response and determine if further action is needed in the public interest, taking into account whether a *reasonable and informed third party* would believe that the auditor has acted appropriately.

Further action could include disclosing the matter to appropriate authorities even if there is no legal obligation to do so and, depending on the situation, withdrawing from the engagement. Withdrawing is not a substitute for taking required actions.

- Document how they fulfilled their responsibilities, including their judgments, actions, and the client’s response.
- Additional requirements apply if the audit is part of a group engagement.

PAPP ENGAGED IN WORK OTHER THAN AUDITS & REVIEWS:

If illegal transactions are identified or suspected by a PAPP providing tax, valuation, or other professional services they would be expected to:

- Seek to obtain an understanding of the matter.
- Discuss the matter with the appropriate level of management or, if they determined that senior management was involved, discuss it with those charged with governance (such as the board of directors).
- Communicate the matter to the auditor, if appropriate. This will depend on consideration of factors such as:
 - Relevant laws and regulations.
 - Whether the audit is being performed by the same firm.
 - Whether the Board has disclosed the matter to the auditor.
- Determine whether further action is needed in the public interest.



SPEAK OUT

REPORTING TO AUTHORITIES: PAs need to understand and comply with legal and regulatory provisions in their jurisdiction, such as requirements to report the matter to authorities, or prohibitions against alerting the organization that action is being taken.

In case of an imminent breach of a law or regulation that would cause substantial harm to investors, creditors, employees, or the general public, the PAPP may decide to immediately disclose the matter to an appropriate authority in order to mitigate the consequences of such a breach.

WHERE TO GET ASSISTANCE?



The NOCLAR provisions for PAPPs are found in **Section 360**. The IESBA **Support & Resources** webpage includes helpful guidance for PAPPs, including a NOCLAR Fact Sheet, IESBA Staff Q&As and videos that explain NOCLAR from a variety of perspectives. Also, the IESBA website includes a comprehensive **NOCLAR webpage**.



The eCode, which is available at www.IESBAeCode.org, is an on-line resource for accountants and other users of the Code. It provides quick and efficient access to the Code, making it easier to use, implement, and enforce.