Federation of European Accountants
Fédération des Experts comptables Européens

Kathleen Healy
Technical Director, IAASB

Posted as comment on:
www.ifac.org

14 October 2015

Dear Ms Healy,

Re: FEE comments on the IAASB's Exposure Draft (ED): "Responding to Non Compliance or Suspected Non Compliance with Laws and Regulations"

FEE (the Federation of European Accountants) is pleased to provide you with its comments on the IAASB Exposure Draft (ED): "Responding to Non Compliance or Suspected Non Compliance with Laws and Regulations" ("the ED" or "ISA 250").

FEE has noted this project by the IAASB, and appreciates the effort to ensure consistency between IAASB's International Standards on Auditing (ISAs) and the IESBA Code of Ethics (the Code), in light of the recent IESBA ED on Responding to Non-Compliance with Laws and Regulations (NOCLAR) issued in May 2015. It is important to consider this response in the context of the FEE response to the IESBA ED on NOCLAR, it is therefore attached as an Appendix to this letter.

Although there may be technical merit in opening up existing ISAs for incremental improvement, we highlight the importance of a cost-benefit analysis to these decisions. Frequent changes to ISAs, which require retranslation and transposition into local law or local standards, create a significant time commitment and cost burden for many jurisdictions. We request that the IAASB consider whether limited changes to ISAs merit such an investment.

FEE has some concern regarding the implicit assumption by the IAASB as to the outcome of the ongoing IESBA consultation. The explanatory memorandum does not indicate the due process in place to ensure a structured communication between the IAASB and IESBA with regard to this ED. Ideally, it would have seemed preferable for the IESBA's proposals to have been fully finalised – following appropriate consultation between the two Boards – prior to the IAASB considering the effect on the ISAs. As noted above, considering them earlier in this process may be perceived as implying full IAASB's support for the IESBA's current proposals. This also results in difficulties for commentators, who still may be considering the merits of the fundamentals of the NOCLAR IESBA's project, rather than purely its application to ISAs.

With this in mind, it may be likely that there will be a need for further amendments following the final changes to the IESBA's proposals. FEE is concerned that the need for consistency between the Code and the IAASB standards has not yet received sufficient focus; FEE would urge the two Boards to continue working together in this regard.

Additionally, some concepts included in the IESBA's proposals relate to accountants who are not involved in audits or other areas dealt with by the IAASB's standards (it includes for instance professional accountants in business). Therefore a part of the reproduced text may not be appropriate or relevant to auditing standards. For example, including a category for "securities, markets and trading" might create unrealistic expectations of what is anticipated from professional accountants in the course of conducting e.g. an audit, assurance or other related services engagement.

If the Code were changed to require instances of NOCLAR that a professional accountant believes may be about to occur[1], this potentially significantly extends the scope of an audit. FEE is of the view that determining whether to disclose a matter to an appropriate authority, and, as a result, breaching client confidentiality, is a matter for legislation, and not for international standard setters to define.

As a general principle, FEE would like the IAASB to avoid repeating the principles of the Code in the ISAs. The Code is designed to be applied in a different way and, while impacting on the ISAs, has a much wider application. Rather, the IAASB should focus on clarifying and providing guidance on the application of the Code, where relevant, to the relevant standards.

For further information on this FEE[2] letter, please contact Noémi Robert on +32 2 893 33 80 or via e-mail at noemi.robert@fee.be from the FEE team.

Yours sincerely,

Petr Kriz
President

Olivier Boutellis-Taft
Chief Executive

[1] Reference is made to proposed Section 225 paragraph 12 of the Code

[2] FEE is the Fédération des Experts comptables Européens (Federation of European Accountants). It represents 47 professional institutes of accountants and auditors from 36 European countries, including all of the 28 European Union (EU) Member States. In representing the European accountancy profession, FEE recognises the public interest. It has a combined membership of more than 800.000 professional accountants, working in different capacities in public practice, small and big firms, government and education, who all contribute to a more efficient, transparent and sustainable European economy.

Appendix 1: Request for specific comments

1. **Whether respondents believe the proposed limited amendments are sufficient to resolve actual or perceived inconsistencies of approach or to clarify and emphasize key aspects of the NOCLAR proposals in the IAASB's International Standards.**

Even with limited amendments, FEE notes that there is still scope for further alignment of the ED with the IESBA ED on NOCLAR, both in terms of the requirements set out, but also in terms of wording and semantics. This is particularly noticable in paragraphs 18-21 of the ISA 250 requirements. Differences in wording between the Code and the ED could lead to uncertainty in their interpretation. The issue of differing interpretations will only be further exacerbated by the translation of the relevant ISAs in different languages and jurisdictions. There is a risk that the various interpretations will lead to an incongruence between ethical standards and auditing standards, and as such, result in disparity and confusion in terms of application.

FEE understands the considerations of the IAASB to incorporate the new paragraph 8 (a). Nevertheless, FEE believes that this addition risks introducing more uncertainty as to what "additional responsibilities" may entail.

FEE does not believe that the IAASB's proposal to change the word "responsibilities" to read "legal or ethical duty or right" is the right approach. It is not clear what an "ethical duty or right" is (paragraph 11 (a) of the introduction), and as such this change introduces further uncertainty (reference is made to Appendix 2 in this respect). Without being clearly defined, which is perhaps not possible, this new concept should not be used and we would favour keeping the commonly understood term "responsibilities". Even if clearly defined, this also risks adding ambiguity in application due to the fact that, although specific laws in jurisdictions differ, generally there is some form of legal confidentiality constraint on reporting both internally and externally on the entitiy. For example, in some cases it is prohibited to alert the entity ("tipping-off") when the auditor is required to report non-compliance to the appropriate authority. As already stated, FEE is of the view that determining whether to disclose a matter to an appropriate authority, and breach client confidentiality, is a matter for legislation, and not for international standard setters to define.

FEE welcomes the inclusion of examples of circumstances "that may cause the auditor to evaluate the implications of non-compliance on the reliability of written representations received from management" within A17- A18a of the explanatory material of the ED. The ED proceeds to discuss procedures that auditors could employ as part of their evaluation. It might also be valuable to explicitly note that the matters which might not directly impact the financial statements, but which may nevertheless cast doubt on management integrity, should also be included in the auditors' evaluation.

It would be pertinent for the respective Boards to ensure an appropriate alignment of the work effort required by the Code and the ISAs, as well as all the other IAASB standards. Alignment and guidance for ISRE 2410, ISAEs 3000, 3400, 3410, 3420, and ISRSs 4400 and 4410 appears to be needed. In addition, IESBA should not include auditing or assurance standards in its Code. The requirements that need to be followed in an audit or assurance engagement should be included in the standards issued by the IAASB. FEE refers to its comment letter submitted to IESBA in this context.

2. The impact, if any, of the proposed limited amendments in jurisdictions that have not adopted, or do not plan to adopt, the IESBA Code. For example, would any of the changes to the IAASB's International Standards be deemed incompatible with the relevant ethical requirements that would apply in those jurisdictions?

Clearly, if aspects of the IESBA Code are included within the ISA then, where jurisdictions have not adopted the Code, this could have an impact on compliance with ISAs, and specifically with the statement in ISA 200 paragraph A14, which notes: "relevant ethical requirements ordinarily comprise Parts A and B of the Code of Ethics for Professional Accountants […], together with national requirements that are more restrictive".

FEE believes that members of the Forum of Firms would not be significantly impacted by this proposal due to their existing obligations. However, for other networks, individual non-network firms and sole practitioners injurisdictions that have not adopted the IESBA Code, the impact could be significant. An impact assessment should be carried out by the IAASB to ensure that no unintended consequences will derive from these limited amendments.

Comments on the general matters:

(a) Translations—Recognizing that many respondents may intend to translate the final amendments to its International Standards for adoption in their own environments, the IAASB welcomes comment on potential translation issues respondents may note in reviewing the proposed amendments to its International Standards.

FEE members are increasingly concerned with the frequency of revisions to IAASB's literature. The resulting retranslation and application, including the effect on any additional local guidance, can be significant. We request that the IAASB consider whether limited changes merit such an investment.

(b) Effective Date—it is anticipated that the effective date of the amendments to the IAASB's International Standards would be aligned with the effective date of the NOCLAR standards, which the IESBA will determine in due course.

FEE notes that there is still scope for further alignment of the ED with the IESBA ED on NOCLAR, both in terms of the requirements set out but also in terms of wording and semantics. FEE would like to emphasise the importance of due process in ensuring alignment in substance, as well as of effective dates. FEE strongly urges cooperation between the two Boards on these two projects.

Appendix 2: FEE comment letter on the IESBA exposure draft: "Responding to Non-Compliance with Laws and Regulations

Mr. Ken Siong
Technical Director
International Ethics Standards Board for Accountants (IESBA)

Email: kensiong@ethicsboard.org

9 September 2015

Dear Mr. Siong,

Re: FEE comments on the IESBA Exposure Draft: "Responding to Non-Compliance with Laws and Regulations"

FEE (the Federation of European Accountants) is pleased to provide you with its comments on the IESBA Exposure Draft "Responding to Non-Compliance with Laws and Regulations" (NOCLAR) ("the ED") proposing amendments to the IESBA Code of Ethics for Professional Accountants ("the Code").

The ED is a significant improvement from the former ED on Responding to a Suspected Illegal Act. It has gone some way to finding a good balance between responding to stakeholders' expectations and complying with the applicable legal framework. The proposals find a sensible approach about each party's responsibilities and recognise the important differences between the role of auditors and the one of other professional accountants in public practice in relation to issues such as client privilege.

FEE agrees with IESBA that the Code is not meant to override national law, and should be applied without prejudice to any applicable legal provisions. FEE welcomes the fact that the Board takes this matter seriously and that a reference to this is now clearly included in the proposed Section 225.27 as "disclosure would be precluded if it would be contrary to law or national regulation". In FEE's view, this is an essential clarification that ought to be more prominent in the finalised Code.

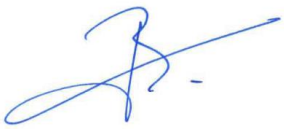
FEE has consistently supported the concept of transparency in its public policy work while recognising limits and practical difficulties that could arise when applying this concept. FEE had previously expressed the opinion that IESBA should not seek to require disclosure in the absence of an appropriate legal framework and retains this stance. FEE is therefore pleased that mandatory reporting is no longer being considered, as this would have resulted in unintended and adverse consequences, potentially reducing the ability of PAs to influence potential non-compliance. FEE would also welcome that the Code clarify that disclosure is precluded where there is a conflict with local laws and regulations, an example being tipping-off concerns under anti-money laundering legislation where a discussion with management may not always be lawfully allowed.

In addition, it should be noted that, in certain circumstances, the reinforcement of the "third party test" included in Section 225.25 could dictate disclosure as the only course of action and thus could create a conflict with the applicable laws and regulations. FEE retains its previously stated position that national laws and regulations, and not IESBA, should deal with breaking client confidentiality.

We would like to draw special attention to those accountants in small and medium practices (SMPs). We appreciate that Section 100.26 of the Code on Communicating with Those Charged with Governance (TCWG) has been adapted for use in a small or medium-sized enterprise (SME). However, on assessing what is reasonable to ask of PAs working in SMPs or SMEs when they come across an act or suspected act of NOCLAR, some requirements and guidance as currently drafted may be seen as complicated to apply in practice in such entities due to a lack of segregation of duties, and the increased potential for management override of controls. Professional judgement would need to be strongly emphasised to those PAs to ensure the application of a proportionate approach.

For further information on this FEE[1] letter, please contact Hilde Blomme on +32 2 893 33 77 or via email at hilde.blomme@fee.be or Noémi Robert on +32 2 893 33 80 or via email at noemi.robert@fee.be.

Yours sincerely,



Petr Kříž
President

Olivier Boutellis-Taft
CEO

[1] FEE is the Fédération des Experts comptables Européens (Federation of European Accountants). It represents 47 professional institutes of accountants and auditors from 36 European countries, including all 28 EU member states. In representing the European accountancy profession, FEE recognises the public interest. It has a combined membership of more than 800,000 professional accountants working in different capacities in public practice, small and large firms, government and education – all of whom contribute to a more efficient, transparent and sustainable European economy.

Appendix - Request for Specific Comments in the IESBA Exposure Draft: "Responding to Non - Compliance with Laws and Regulations"

Question 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?

Providing guidance to PAs on how they may react in instances of NOCLAR or suspected NOCLAR was the intention of the original project. The IESBA Code is not meant to override national law, and should be applied without prejudice to any applicable legal provisions in any jurisdiction conferring a right to override confidentiality. FEE welcomes the fact that the Board takes this matter seriously and that a reference to this is now clearly included in the ED as "disclosure would be precluded if it would be contrary to law or national regulation". In FEE's view, this is an essential clarification, which ought to be more prominent in the finalised Code. To do so, section 225.12 could be clarified if it started with "Subject to the content of paragraph 225.10, [...]" .

As emphasised in the covering letter, FEE has consistently supported the concept of transparency in its public policy work while recognising limits and practical difficulties that could arise when applying this concept. FEE had previously expressed the opinion that IESBA should not seek to require disclosure in the absence of an appropriate legal framework and retains this stance. FEE is therefore pleased to note that mandatory reporting is no longer being considered, as this would have resulted in unintended and adverse consequences, potentially reducing the ability of PAs to influence potential non-compliance. FEE would also be pleased if the Code could clarify that disclosure is precluded where there is a conflict with local laws and regulations, an example being tipping-off concerns under anti-money laundering legislation where a discussion with management may not always be lawfully allowed.

FEE supports the fact that the proposals require PAs to obtain an understanding of the applicable regulation. This should help lead to consistent application by all PAs in jurisdictions where such disclosure requirements exist.

Question 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?

FEE fully subscribes to the importance of the public interest for the credibility of the accountancy profession and is supportive of frameworks and initiatives in relation to PA's duty to "act in the public interest". FEE also recognises the efforts made by the Board in addressing public interest issues of subjectivity and differing approaches by introducing the concept of substantial harm to interests of stakeholders or the wider public.

Nevertheless, the concept has not been developed sufficiently enough to enable it to address the differing public interest expectations. This concept will not prove workable in practice without detailed criteria as to how it can be assessed. Care should be taken to avoid the phrase being used as a way of extending general law enforcement responsibilities to the profession as a whole. As an example, from paragraph 50 onwards, IESBA rightly acknowledges that "public interest" is "too broad and vague" as a threshold. In Section 225.4, IESBA nonetheless tries to determine what constitutes the public interest, and in Section 225.25 the "third party test", which is already a proxy, refers to the broad and vague concept of public interest as the benchmark for the PA's judgement. Such subjective concepts cannot, in our view, be properly addressed in a Code with an international remit, and any attempt to do so could lead to inconsistent application and prove unworkable.

Question 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:

As a respondent from the "other" category, FEE emphasises the impact of the practical aspects of the proposals, particularly on the relationships between:

a. Auditors and audited entities;

FEE anticipates that the effect on audits carried out under ISAs would be negligible, given the requirements under ISA 250. Nevertheless, FEE is asking IESBA to be mindful not to go beyond the requirements of the ISAs. For transparency of the relationship with the audited entity, the proposals should be clear enough so as not to create uncertainty as to what and when auditors should report externally.

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

FEE believes that the proposals recognise the important difference between the role of auditors and that of PAs in public practice that provide services other than audits. It also takes into consideration issues such as client privilege.

c. PAIBs and their employing organizations.

The proposals take a reasonable approach to the expectations of PAIBs to report on NOCLAR at their employer. PAIBs may have difficulties in deterring prospective or suspected NOCLAR, in instances where this has not yet occurred. The responsibility of PAIBs should not go beyond explaining the expected breach and its consequences to management or TCWG, including the effective delivery of good advice.

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

FEE is broadly supportive of the proposed objectives for all categories of PAs as set out in Section 225.3. Whilst we agree in principle with the intention of "(c) To take further action as may be needed in the public interest", we are concerned that this sentence may be too wide and be responded to with divergent interpretations. In this regard, we refer to our general comments in the covering letter.

We also refer to our response to Question 6.

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

FEE recognises that ISA 250 has formed the basis for the scope of laws and regulations covered in Sections 225 and 360. FEE is pleased that improvements have been made in comparison to the previous ED in aligning the Code to ISA 250 and is also duly following the project of the IAASB to revise ISA 250. It is instrumental for FEE that the wording of both texts be aligned to avoid any misunderstanding and differences in application. In addition, the Code should reflect the information concerning the inherent limitations recognised in paragraph 5 of ISA 250 in order to inform public expectations about the ability of the auditor to react to NOCLAR. In addition, whereas ISAs take a risk-based approach, this aspect may not be sufficiently clear in the Code.

In respect of Section 360, FEE has some reservations as to the ability of PAIBs in this regard. Depending on their background, their training may not equip them to deal with this adequately. For these PAs, any ability to identify NOCLAR is linked to the nature and scope of their individual roles in the organisation, which can be very narrow and limited. This could be made clearer in the proposals. Moreover, in parallel, public expectations will increase, which may therefore not be able to be met in all instances. This could ultimately be detrimental to the profession's reputation.

Sections 225.29, 225.45 and 360.28 state that "If the professional accountant determines that disclosure of the matter to an appropriate authority is an appropriate course of action in the circumstances, this will not be considered a breach of the duty of confidentiality under Section 140 of the Code". FEE is concerned that this wording is misleading as, under national law, disclosure could be forbidden. As such, one might not be aware upon reading the Code that disclosure would potentially be a breach of national law. FEE retains its previously stated position that national laws and regulations, and not IESBA, should deal with breaking auditor's client confidentiality.

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

FEE is broadly supportive of the proposed categories of PAs with some reservations as to the work effort foreseen for PAIBs and other PAs who are not auditors. These categories of PAs do not have the same degree of public interest mandate as auditors, and it is therefore unrealistic to expect them to undertake essentially similar procedures in relation to NOCLAR.

Regarding PAIBs specifically, their role and the responsibility that comes with it are factors that influence what the public expects them to do. The higher the position in the organisation, the more authority and the more scope one has to escalate a NOCLAR, or suspected NOCLAR. Therefore, it is logical to place higher expectations on senior PAIBs than non-senior PAIBs. However, we can foresee difficulties in distinguishing between these two arbitrary categories. This could potentially lead to regulatory implications in the future.

In addition, PAIBs may have difficulties in deterring prospective or suspected NOCLAR, in instances where this has not yet occurred. The responsibility of PAIBs should be limited to explaining the expected breach and its consequences to management or TCWG, including the effective delivery of good advice.

Question 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?

FEE deems that the factors to consider could be revised further to avoid too much uncertainty in their interpretation. The interaction between the factors also needs to be considered in order to ensure that the required determination is not disproportionate and unnecessarily complex. For example, "urgency of the matter" is not always clearly discernible, and what would be the degree of urgency that would "cross the threshold"?

We suggest that IESBA explicitly makes reference to instances where there is no credible evidence but only a suspicion of NOCLAR, and as such refer to the steps which a PA would be anticipated to follow in assessing the potential consequences (for example reputational damage) of any action taken. In such circumstances, the risk of an incorrect assessment of the situation is more probable and could have severe reputational and potentially financial consequences for the PA.

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?

The imposition of the "third party test" is intended to provide a basis for establishing a framework to ensure the objective and rigorous assessment for determining the need for, and nature and extent of, further action. It should be emphasised though that what is deemed to be a "reasonable and informed third party" is subjective, as is the term "acting in the public interest". Such subjective concepts cannot be properly addressed within a Code with an international remit, and any attempt to do so could lead to inconsistent application and render the provisions in the Code unworkable.

FEE is not comfortable with the fact that the "third party test", which is already a proxy, refers to the broad and vague concept of public interest as the benchmark for the PA's judgement. Subjectivity will always remain a factor in this assessment, and interpretation is likely to vary in different jurisdictions. What a reasonable and informed third party expects a PA to do depends on the specific facts and circumstances, and one's role and position at that time. It is not straightforward to apply, especially for PAs in public practice providing services other than audits.

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?

The proposals do not provide any flexibility to take into account differing circumstances. For FEE, the reinforcement of the "third party test" dictates disclosure as the course of action and thus, if applicable, this forces the auditor to break client confidentiality. It may lead to a "de-facto" requirement in some severe cases and a large amount of uncertainty in many others, making the proposals potentially detrimental to the entire profession.

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

Providing guidance to PAs on how they may react in instances of NOCLAR or suspected NOCLAR was the intention of the original project. FEE is of the view that breaching client confidentiality is a matter for legislation, and not for an international Ethics Code.

FEE agrees that a list of factors may be useful to PAs in deciding whether there is a need to terminate a relationship with a client or an employer.

Question 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?

According to the revised proposals, the disclosure of the information to the audit partner is required when a PA in public practice provides services other than audits to an audit client of that same firm. There is no explicit requirement to disclose the information to the auditor of a network firm. This seems to be a proportionate solution to deal with confidentiality and privacy laws. However, the ED does not address how to deal with situations which arise as part of cross-border engagements, including group audit situations. This is particularly problematic in jurisdictions which have laws with extraterritorial outreach. This aspect needs to be looked at further before these proposals are finalised.

We wonder whether Section 225.43 is applicable in the case of a group audit in which several different audit organisations (not network firms) are involved. This should be clarified.

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

We agree with the proportionate approach taken to documentation, where auditors are required to document and other PAs in public practice, as well as PAIBs are encouraged to do so.