

INTERNATIONAL STANDARD ON AUDITING 250 (REVISED)
CONSIDERATION OF LAWS AND REGULATIONS IN AN
AUDIT OF FINANCIAL STATEMENTS

(Effective for audits of financial statements for periods beginning
on or after December 15, 2017)

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International Standard on Auditing (ISA) 250 (Revised), *Consideration of Laws and Regulations in an Audit of Financial Statements*, should be read in conjunction with ISA 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing*.

Introduction

Scope of this ISA

1. This International Standard on Auditing (ISA) deals with the auditor's responsibility to consider laws and regulations in an audit of financial statements. This ISA does not apply to other assurance engagements in which the auditor is specifically engaged to test and report separately on compliance with specific laws or regulations.

Effect of Laws and Regulations

2. The effect on financial statements of laws and regulations varies considerably. Those laws and regulations to which an entity is subject constitute the legal and regulatory framework. The provisions of some laws or regulations have a direct effect on the financial statements in that they determine the reported amounts and disclosures in an entity's financial statements. Other laws or regulations are to be complied with by management or set the provisions under which the entity is allowed to conduct its business but do not have a direct effect on an entity's financial statements. Some entities operate in heavily regulated industries (such as banks and chemical companies). Others are subject only to the many laws and regulations that relate generally to the operating aspects of the business (such as those related to occupational safety and health, and equal employment opportunity). Non-compliance with laws and regulations may result in fines, litigation or other consequences for the entity that may have a material effect on the financial statements.

Responsibility for Compliance with Laws and Regulations (Ref: Para. A1–A8)

3. It is the responsibility of management, with the oversight of those charged with governance, to ensure that the entity's operations are conducted in accordance with the provisions of laws and regulations, including compliance with the provisions of laws and regulations that determine the reported amounts and disclosures in an entity's financial statements.

Responsibility of the Auditor

4. The requirements in this ISA are designed to assist the auditor in identifying material misstatement of the financial statements due to non-compliance with laws and regulations. However, the auditor is not responsible for preventing non-compliance and cannot be expected to detect non-compliance with all laws and regulations.
5. The auditor is responsible for obtaining reasonable assurance that the financial statements, taken as a whole, are free from material misstatement, whether due to fraud or error.¹ In conducting an audit of financial statements, the auditor

¹ ISA 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing*, paragraph 5

takes into account the applicable legal and regulatory framework. Owing to the inherent limitations of an audit, there is an unavoidable risk that some material misstatements in the financial statements may not be detected, even though the audit is properly planned and performed in accordance with the ISAs.² In the context of laws and regulations, the potential effects of inherent limitations on the auditor's ability to detect material misstatements are greater for such reasons as the following:

- There are many laws and regulations, relating principally to the operating aspects of an entity, that typically do not affect the financial statements and are not captured by the entity's information systems relevant to financial reporting.
- Non-compliance may involve conduct designed to conceal it, such as collusion, forgery, deliberate failure to record transactions, management override of controls or intentional misrepresentations being made to the auditor.
- Whether an act constitutes non-compliance is ultimately a matter to be determined by a court or other appropriate adjudicative body.

Ordinarily, the further removed non-compliance is from the events and transactions reflected in the financial statements, the less likely the auditor is to become aware of it or to recognize the non-compliance.

6. This ISA distinguishes the auditor's responsibilities in relation to compliance with two different categories of laws and regulations as follows: (Ref: Para. A6, A12–A13)
 - (a) The provisions of those laws and regulations generally recognized to have a direct effect on the determination of material amounts and disclosures in the financial statements such as tax and pension laws and regulations (see paragraph 14) (Ref: Para. A12); and
 - (b) Other laws and regulations that do not have a direct effect on the determination of the amounts and disclosures in the financial statements, but compliance with which may be fundamental to the operating aspects of the business, to an entity's ability to continue its business, or to avoid material penalties (e.g., compliance with the terms of an operating license, compliance with regulatory solvency requirements, or compliance with environmental regulations); non-compliance with such laws and regulations may therefore have a material effect on the financial statements (see paragraph 15) (Ref: Para. A13).
7. In this ISA, differing requirements are specified for each of the above categories of laws and regulations. For the category referred to in paragraph 6(a), the auditor's responsibility is to obtain sufficient appropriate audit evidence regarding

² ISA 200, paragraphs A53–A54

compliance with the provisions of those laws and regulations. For the category referred to in paragraph 6(b), the auditor's responsibility is limited to undertaking specified audit procedures to help identify non-compliance with those laws and regulations that may have a material effect on the financial statements.

8. The auditor is required by this ISA to remain alert to the possibility that other audit procedures applied for the purpose of forming an opinion on financial statements may bring instances of non-compliance to the auditor's attention. Maintaining professional skepticism throughout the audit, as required by ISA 200,³ is important in this context, given the extent of laws and regulations that affect the entity.
9. The auditor may have additional responsibilities under law, regulation or relevant ethical requirements regarding an entity's non-compliance with laws and regulations, which may differ from or go beyond this ISA, such as: (Ref: Para. A8)
 - (a) Responding to identified or suspected non-compliance with laws and regulations, including requirements in relation to specific communications with management and those charged with governance, assessing the appropriateness of their response to non-compliance and determining whether further action is needed;
 - (b) Communicating identified or suspected non-compliance with laws and regulations to other auditors (e.g., in an audit of group financial statements); and
 - (c) Documentation requirements regarding identified or suspected non-compliance with laws and regulations.

Complying with any additional responsibilities may provide further information that is relevant to the auditor's work in accordance with this and other ISAs (e.g., regarding the integrity of management or, where appropriate, those charged with governance).

Effective Date

10. This ISA is effective for audits of financial statements for periods beginning on or after December 15, 2017.

Objectives

11. The objectives of the auditor are:
 - (a) To obtain sufficient appropriate audit evidence regarding compliance with the provisions of those laws and regulations generally recognized to have a direct effect on the determination of material amounts and disclosures in the financial statements;

³ ISA 200, paragraph 15

- (b) To perform specified audit procedures to help identify instances of non-compliance with other laws and regulations that may have a material effect on the financial statements; and
- (c) To respond appropriately to identified or suspected non-compliance with laws and regulations identified during the audit.

Definition

12. For the purposes of this ISA, the following term has the meaning attributed below:

Non-compliance – Acts of omission or commission, intentional or unintentional, committed by the entity, or by those charged with governance, by management or by other individuals working for or under the direction of the entity, which are contrary to the prevailing laws or regulations. Non-compliance does not include personal misconduct unrelated to the business activities of the entity. (Ref: Para. A9–A10)

Requirements

The Auditor's Consideration of Compliance with Laws and Regulations

13. As part of obtaining an understanding of the entity and its environment in accordance with ISA 315 (Revised),⁴ the auditor shall obtain a general understanding of:
- (a) The legal and regulatory framework applicable to the entity and the industry or sector in which the entity operates; and
 - (b) How the entity is complying with that framework. (Ref: Para. A11)
14. The auditor shall obtain sufficient appropriate audit evidence regarding compliance with the provisions of those laws and regulations generally recognized to have a direct effect on the determination of material amounts and disclosures in the financial statements. (Ref: Para. A12)
15. The auditor shall perform the following audit procedures to help identify instances of non-compliance with other laws and regulations that may have a material effect on the financial statements: (Ref: Para. A13–A14)
- (a) Inquiring of management and, where appropriate, those charged with governance, as to whether the entity is in compliance with such laws and regulations; and
 - (b) Inspecting correspondence, if any, with the relevant licensing or regulatory authorities.

⁴ ISA 315 (Revised), *Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment*, paragraph 11

16. During the audit, the auditor shall remain alert to the possibility that other audit procedures applied may bring instances of non-compliance or suspected non-compliance with laws and regulations to the auditor's attention. (Ref: Para. A15)
17. The auditor shall request management and, where appropriate, those charged with governance, to provide written representations that all known instances of non-compliance or suspected non-compliance with laws and regulations whose effects should be considered when preparing financial statements have been disclosed to the auditor. (Ref: Para. A16)
18. In the absence of identified or suspected non-compliance, the auditor is not required to perform audit procedures regarding the entity's compliance with laws and regulations, other than those set out in paragraphs 13–17.

Audit Procedures When Non-Compliance Is Identified or Suspected

19. If the auditor becomes aware of information concerning an instance of non-compliance or suspected non-compliance with laws and regulations, the auditor shall obtain: (Ref: Para. A17–A18)
 - (a) An understanding of the nature of the act and the circumstances in which it has occurred; and
 - (b) Further information to evaluate the possible effect on the financial statements. (Ref: Para. A19)
20. If the auditor suspects there may be non-compliance, the auditor shall discuss the matter, unless prohibited by law or regulation, with the appropriate level of management and, where appropriate, those charged with governance. If management or, as appropriate, those charged with governance do not provide sufficient information that supports that the entity is in compliance with laws and regulations and, in the auditor's judgment, the effect of the suspected non-compliance may be material to the financial statements, the auditor shall consider the need to obtain legal advice. (Ref: Para. A20–A22)
21. If sufficient information about suspected non-compliance cannot be obtained, the auditor shall evaluate the effect of the lack of sufficient appropriate audit evidence on the auditor's opinion.
22. The auditor shall evaluate the implications of identified or suspected non-compliance in relation to other aspects of the audit, including the auditor's risk assessment and the reliability of written representations, and take appropriate action. (Ref: Para. A23–A25)

Communicating and Reporting Identified or Suspected Non-Compliance

Communicating Identified or Suspected Non-Compliance with Those Charged with Governance

23. Unless all of those charged with governance are involved in management of the entity, and therefore are aware of matters involving identified or suspected

non-compliance already communicated by the auditor,⁵ the auditor shall communicate, unless prohibited by law or regulation, with those charged with governance matters involving non-compliance with laws and regulations that come to the auditor's attention during the course of the audit, other than when the matters are clearly inconsequential.

24. If, in the auditor's judgment, the non-compliance referred to in paragraph 23 is believed to be intentional and material, the auditor shall communicate the matter with those charged with governance as soon as practicable.
25. If the auditor suspects that management or those charged with governance are involved in non-compliance, the auditor shall communicate the matter to the next higher level of authority at the entity, if it exists, such as an audit committee or supervisory board. Where no higher authority exists, or if the auditor believes that the communication may not be acted upon or is unsure as to the person to whom to report, the auditor shall consider the need to obtain legal advice.

Potential Implications of Identified or Suspected Non-Compliance for the Auditor's Report (Ref: Para. A26–A27)

26. If the auditor concludes that the identified or suspected non-compliance has a material effect on the financial statements, and has not been adequately reflected in the financial statements, the auditor shall, in accordance with ISA 705 (Revised), express a qualified opinion or an adverse opinion on the financial statements.⁶
27. If the auditor is precluded by management or those charged with governance from obtaining sufficient appropriate audit evidence to evaluate whether non-compliance that may be material to the financial statements has, or is likely to have, occurred, the auditor shall express a qualified opinion or disclaim an opinion on the financial statements on the basis of a limitation on the scope of the audit in accordance with ISA 705 (Revised).⁷
28. If the auditor is unable to determine whether non-compliance has occurred because of limitations imposed by the circumstances rather than by management or those charged with governance, the auditor shall evaluate the effect on the auditor's opinion in accordance with ISA 705 (Revised).

Reporting Identified or Suspected Non-Compliance to an Appropriate Authority outside the Entity

29. If the auditor has identified or suspects non-compliance with laws and regulations, the auditor shall determine whether law, regulation or relevant ethical requirements: (Ref: Para. A28–A34)

⁵ ISA 260 (Revised), *Communication with Those Charged with Governance*, paragraph 13

⁶ ISA 705 (Revised), *Modifications to the Opinion in the Independent Auditor's Report*, paragraphs 7–8

⁷ ISA 705 (Revised), paragraphs 7 and 9

- (a) Require the auditor to report to an appropriate authority outside the entity.
- (b) Establish responsibilities under which reporting to an appropriate authority outside the entity may be appropriate in the circumstances.

Documentation

30. The auditor shall include in the audit documentation⁸ identified or suspected non-compliance with laws and regulations and: (Ref: Para. A35–A36)
- (a) The audit procedures performed, the significant professional judgments made and the conclusions reached thereon; and
 - (b) The discussions of significant matters related to the non-compliance with management, those charged with governance and others, including how management and, where applicable, those charged with governance have responded to the matter.

Application and Other Explanatory Material

Responsibility for Compliance with Laws and Regulations (Ref: Para. 3–9)

- A1. It is the responsibility of management, with the oversight of those charged with governance, to ensure that the entity's operations are conducted in accordance with laws and regulations. Laws and regulations may affect an entity's financial statements in different ways: for example, most directly, they may affect specific disclosures required of the entity in the financial statements or they may prescribe the applicable financial reporting framework. They may also establish certain legal rights and obligations of the entity, some of which will be recognized in the entity's financial statements. In addition, laws and regulations may impose penalties in cases of non-compliance.
- A2. The following are examples of the types of policies and procedures an entity may implement to assist in the prevention and detection of non-compliance with laws and regulations:
- Monitoring legal requirements and ensuring that operating procedures are designed to meet these requirements.
 - Instituting and operating appropriate systems of internal control.
 - Developing, publicizing and following a code of conduct.
 - Ensuring employees are properly trained and understand the code of conduct.

⁸ ISA 230, *Audit Documentation*, paragraphs 8–11, and A6

- Monitoring compliance with the code of conduct and acting appropriately to discipline employees who fail to comply with it.
- Engaging legal advisors to assist in monitoring legal requirements.
- Maintaining a register of significant laws and regulations with which the entity has to comply within its particular industry and a record of complaints.

In larger entities, these policies and procedures may be supplemented by assigning appropriate responsibilities to the following:

- An internal audit function.
- An audit committee.
- A compliance function.

Responsibility of the Auditor

- A3. Non-compliance by the entity with laws and regulations may result in a material misstatement of the financial statements. Detection of non-compliance, regardless of materiality, may affect other aspects of the audit including, for example, the auditor's consideration of the integrity of management, those charged with governance or employees.
- A4. Whether an act constitutes non-compliance with laws and regulations is a matter to be determined by a court or other appropriate adjudicative body, which is ordinarily beyond the auditor's professional competence to determine. Nevertheless, the auditor's training, experience and understanding of the entity and its industry or sector may provide a basis to recognize that some acts, coming to the auditor's attention, may constitute non-compliance with laws and regulations.
- A5. In accordance with specific statutory requirements, the auditor may be specifically required to report, as part of the audit of the financial statements, on whether the entity complies with certain provisions of laws or regulations. In these circumstances, ISA 700 (Revised)⁹ or ISA 800 (Revised)¹⁰ deal with how these audit responsibilities are addressed in the auditor's report. Furthermore, where there are specific statutory reporting requirements, it may be necessary for the audit plan to include appropriate tests for compliance with these provisions of the laws and regulations.

Categories of Laws and Regulations (Ref: Para. 6)

- A6. The nature and circumstances of the entity may impact whether relevant laws and regulations are within the categories of laws and regulations described in

⁹ ISA 700 (Revised), *Forming an Opinion and Reporting on Financial Statements*, paragraph 43

¹⁰ ISA 800 (Revised), *Special Considerations—Audits of Financial Statements Prepared in Accordance with Special Purpose Frameworks*, paragraph 11

paragraphs 6(a) or 6(b). Examples of laws and regulations that may be included in the categories described in paragraph 6 include those that deal with:

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

Considerations Specific to Public Sector Entities

- A7. In the public sector, there may be additional audit responsibilities with respect to the consideration of laws and regulations which may relate to the audit of financial statements or may extend to other aspects of the entity's operations.

Additional Responsibilities Established by Law, Regulation or Relevant Ethical Requirements (Ref: Para. 9)

- A8. Law, regulation or relevant ethical requirements may require the auditor to perform additional procedures and take further actions. For example, the International Ethics Standards Board for Accountants' *International Code of Ethics for Professional Accountants (including International Independence Standards)* (IESBA Code) requires the auditor to take steps to respond to identified or suspected non-compliance with laws and regulations and determine whether further action is needed. Such steps may include the communication of identified or suspected non-compliance with laws and regulations to other auditors within a group, including a group engagement partner, component auditors or other auditors performing work at components of a group for purposes other than the audit of the group financial statements.¹¹

Definition (Ref: Para. 12)

- A9. Acts of non-compliance with laws and regulations include transactions entered into by, or in the name of, the entity, or on its behalf, by those charged with governance, by management or by other individuals working for or under the direction of the entity.
- A10. Non-compliance also includes personal misconduct related to the business activities of the entity, for example, in circumstances where an individual in a

¹¹ See, for example, paragraphs R360.16–360.18 A1 of the IESBA Code.

key management position, in a personal capacity, has accepted a bribe from a supplier of the entity and in return secures the appointment of the supplier to provide services or contracts to the entity.

The Auditor's Consideration of Compliance with Laws and Regulations

Obtaining an Understanding of the Legal and Regulatory Framework (Ref: Para. 13)

A11. To obtain a general understanding of the legal and regulatory framework, and how the entity complies with that framework, the auditor may, for example:

- Use the auditor's existing understanding of the entity's industry, regulatory and other external factors;
- Update the understanding of those laws and regulations that directly determine the reported amounts and disclosures in the financial statements;
- Inquire of management as to other laws or regulations that may be expected to have a fundamental effect on the operations of the entity;
- Inquire of management concerning the entity's policies and procedures regarding compliance with laws and regulations; and
- Inquire of management regarding the policies or procedures adopted for identifying, evaluating and accounting for litigation claims.

Laws and Regulations Generally Recognized to Have a Direct Effect on the Determination of Material Amounts and Disclosures in the Financial Statements (Ref: Para. 6 and 14)

A12. Certain laws and regulations are well-established, known to the entity and within the entity's industry or sector, and relevant to the entity's financial statements (as described in paragraph 6(a)). They could include those that relate to, for example:

- The form and content of financial statements;
- Industry-specific financial reporting issues;
- Accounting for transactions under government contracts; or
- The accrual or recognition of expenses for income tax or pension costs.

Some provisions in those laws and regulations may be directly relevant to specific assertions in the financial statements (e.g., the completeness of income tax provisions), while others may be directly relevant to the financial statements as a whole (e.g., the required statements constituting a complete set of financial statements). The aim of the requirement in paragraph 14 is for the auditor to obtain sufficient appropriate audit evidence regarding the determination of amounts and disclosures in the financial statements in compliance with the relevant provisions of those laws and regulations.

Non-compliance with other provisions of such laws and regulations and other laws and regulations may result in fines, litigation or other consequences for the entity, the costs of which may need to be provided for in the financial statements, but are not considered to have a direct effect on the financial statements as described in paragraph 6(a).

Procedures to Identify Instances of Non-Compliance—Other Laws and Regulations
(Ref: Para. 6 and 15)

- A13. Certain other laws and regulations may need particular attention by the auditor because they have a fundamental effect on the operations of the entity (as described in paragraph 6(b)). Non-compliance with laws and regulations that have a fundamental effect on the operations of the entity may cause the entity to cease operations, or call into question the entity's continuance as a going concern.¹² For example, non-compliance with the requirements of the entity's license or other entitlement to perform its operations could have such an impact (e.g., for a bank, non-compliance with capital or investment requirements). There are also many laws and regulations relating principally to the operating aspects of the entity that typically do not affect the financial statements and are not captured by the entity's information systems relevant to financial reporting.
- A14. As the financial reporting consequences of other laws and regulations can vary depending on the entity's operations, the audit procedures required by paragraph 15 are directed to bringing to the auditor's attention instances of non-compliance with laws and regulations that may have a material effect on the financial statements.

Non-Compliance Brought to the Auditor's Attention by Other Audit Procedures
(Ref: Para. 16)

- A15. Audit procedures applied to form an opinion on the financial statements may bring instances of non-compliance or suspected non-compliance with laws and regulations to the auditor's attention. For example, such audit procedures may include:
- Reading minutes;
 - Inquiring of the entity's management and in-house legal counsel or external legal counsel concerning litigation, claims and assessments; and
 - Performing substantive tests of details of classes of transactions, account balances or disclosures.

Written Representations (Ref: Para. 17)

- A16. Because the effect on financial statements of laws and regulations can vary considerably, written representations provide necessary audit evidence

¹² See ISA 570 (Revised), *Going Concern*.

about management's knowledge of identified or suspected non-compliance with laws and regulations, whose effects may have a material effect on the financial statements. However, written representations do not provide sufficient appropriate audit evidence on their own and, accordingly, do not affect the nature and extent of other audit evidence that is to be obtained by the auditor.¹³

Audit Procedures When Non-Compliance Is Identified or Suspected

Indications of Non-Compliance with Laws and Regulations (Ref: Para. 19)

- A17. The auditor may become aware of information concerning an instance of non-compliance with laws and regulations other than as a result of performing the procedures in paragraphs 13–17 (e.g., when the auditor is alerted to non-compliance by a whistle blower).
- A18. The following matters may be an indication of non-compliance with laws and regulations:
- Investigations by regulatory organizations and government departments or payment of fines or penalties.
 - Payments for unspecified services or loans to consultants, related parties, employees or government employees.
 - Sales commissions or agent's fees that appear excessive in relation to those ordinarily paid by the entity or in its industry or to the services actually received.
 - Purchasing at prices significantly above or below market price.
 - Unusual payments in cash, purchases in the form of cashiers' checks payable to bearer or transfers to numbered bank accounts.
 - Unusual transactions with companies registered in tax havens.
 - Payments for goods or services made other than to the country from which the goods or services originated.
 - Payments without proper exchange control documentation.
 - Existence of an information system which fails, whether by design or by accident, to provide an adequate audit trail or sufficient evidence.
 - Unauthorized transactions or improperly recorded transactions.
 - Adverse media comment.

Matters Relevant to the Auditor's Evaluation (Ref: Para. 19(b))

- A19. Matters relevant to the auditor's evaluation of the possible effect on the financial statements include:

¹³ ISA 580, *Written Representations*, paragraph 4

- The potential financial consequences of identified or suspected non-compliance with laws and regulations on the financial statements including, for example, the imposition of fines, penalties, damages, threat of expropriation of assets, enforced discontinuation of operations, and litigation.
- Whether the potential financial consequences require disclosure.
- Whether the potential financial consequences are so serious as to call into question the fair presentation of the financial statements, or otherwise make the financial statements misleading.

Audit Procedures and Communicating Identified or Suspected Non-Compliance with Management and Those Charged with Governance (Ref: Para. 20)

- A20. The auditor is required to discuss the suspected non-compliance with the appropriate level of management and, where appropriate, those charged with governance, as they may be able to provide additional audit evidence. For example, the auditor may confirm that management and, where appropriate, those charged with governance have the same understanding of the facts and circumstances relevant to transactions or events that have led to the suspected non-compliance with laws and regulations.
- A21. However, in some jurisdictions, law or regulation may restrict the auditor's communication of certain matters with management and those charged with governance. Law or regulation may specifically prohibit a communication, or other action, that might prejudice an investigation by an appropriate authority into an actual, or suspected, illegal act, including alerting the entity, for example, when the auditor is required to report the identified or suspected non-compliance to an appropriate authority pursuant to anti-money laundering legislation. In these circumstances, the issues considered by the auditor may be complex and the auditor may consider it appropriate to obtain legal advice.
- A22. If management or, as appropriate, those charged with governance do not provide sufficient information to the auditor that the entity is in fact in compliance with laws and regulations, the auditor may consider it appropriate to consult with the entity's in-house or external legal counsel about the application of the laws and regulations to the circumstances, including the possibility of fraud, and the possible effects on the financial statements. If it is not considered appropriate to consult with the entity's legal counsel or if the auditor is not satisfied with the legal counsel's opinion, the auditor may consider it appropriate to consult on a confidential basis with others within the firm, a network firm, a professional body, or with the auditor's legal counsel as to whether a contravention of a law or regulation is involved, including the possibility of fraud, the possible legal consequences, and what further action, if any, the auditor would take.

Evaluating the Implications of Identified or Suspected Non-Compliance
(Ref: Para. 22)

- A23. As required by paragraph 22, the auditor evaluates the implications of identified or suspected non-compliance in relation to other aspects of the audit, including the auditor's risk assessment and the reliability of written representations. The implications of particular identified or suspected non-compliance will depend on the relationship of the perpetration and concealment, if any, of the act to specific control activities and the level of management or individuals working for, or under the direction of, the entity involved, especially implications arising from the involvement of the highest authority within the entity. As noted in paragraph 9, the auditor's compliance with law, regulation or relevant ethical requirements may provide further information that is relevant to the auditor's responsibilities in accordance with paragraph 22.
- A24. Examples of circumstances that may cause the auditor to evaluate the implications of identified or suspected non-compliance on the reliability of written representations received from management and, where applicable, those charged with governance include when:
- The auditor suspects or has evidence of the involvement or intended involvement of management and, where applicable, those charged with governance in any identified or suspected non-compliance.
 - The auditor is aware that management and, where applicable, those charged with governance have knowledge of such non-compliance and, contrary to legal or regulatory requirements, have not reported, or authorized reporting of, the matter to an appropriate authority within a reasonable period.
- A25. In certain circumstances, the auditor may consider withdrawing from the engagement, where permitted by law or regulation, for example when management or those charged with governance do not take the remedial action that the auditor considers appropriate in the circumstances or the identified or suspected non-compliance raises questions regarding the integrity of management or those charged with governance, even when the non-compliance is not material to the financial statements. The auditor may consider it appropriate to obtain legal advice to determine whether withdrawal from the engagement is appropriate. When the auditor determines that withdrawing from the engagement would be appropriate, doing so would not be a substitute for complying with other responsibilities under law, regulation or relevant ethical requirements to respond to identified or suspected non-compliance. Furthermore, paragraph A9 of ISA 220¹⁴ indicates that some ethical requirements may require the predecessor auditor, upon request by the proposed successor auditor, to provide information regarding non-compliance with laws and regulations to the successor auditor.

¹⁴ ISA 220, *Quality Control for an Audit of Financial Statements*

Communicating and Reporting Identified or Suspected Non-Compliance

Potential Implications of Identified or Suspected Non-Compliance for the Auditor's Report (Ref: Para. 26–28)

A26. Identified or suspected non-compliance with laws and regulation is communicated in the auditor's report when the auditor modifies the opinion in accordance with paragraphs 26–28. In certain other circumstances, the auditor may communicate identified or suspected non-compliance in the auditor's report, for example:

- When the auditor has other reporting responsibilities, in addition to the auditor's responsibilities under the ISAs, as contemplated by paragraph 43 of ISA 700 (Revised);
- When the auditor determines that the identified or suspected non-compliance is a key audit matter and accordingly communicates the matter in accordance with ISA 701,¹⁵ unless paragraph 14 of that ISA applies; or
- In exceptional cases when management or those charged with governance do not take the remedial action that the auditor considers appropriate in the circumstances and withdrawal from the engagement is not possible (see paragraph A25), the auditor may consider describing the identified or suspected non-compliance in an Other Matter paragraph in accordance with ISA 706 (Revised).¹⁶

A27. Law or regulation may preclude public disclosure by either management, those charged with governance or the auditor about a specific matter. For example, law or regulation may specifically prohibit a communication, or other action, that might prejudice an investigation by an appropriate authority into an actual, or suspected, illegal act, including a prohibition on alerting the entity. When the auditor intends to communicate identified or suspected non-compliance in the auditor's report under the circumstances set out in paragraph A26 or otherwise, such law or regulation may have implications for the auditor's ability to describe the matter in the auditor's report, or in some circumstances to issue the auditor's report. In such cases, the auditor may consider obtaining legal advice to determine the appropriate course of action.

Reporting Identified or Suspected Non-Compliance to an Appropriate Authority outside the Entity (Ref: Para. 29)

A28. Reporting identified or suspected non-compliance with laws and regulations to an appropriate authority outside the entity may be required or appropriate in the circumstances because:

¹⁵ ISA 701, *Communicating Key Audit Matters in the Independent Auditor's Report*

¹⁶ ISA 706 (Revised), *Emphasis of Matter Paragraphs and Other Matter Paragraphs in the Independent Auditor's Report*

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- (a) Law, regulation or relevant ethical requirements require the auditor to report (see paragraph A29);
- (b) The auditor has determined reporting is an appropriate action to respond to identified or suspected non-compliance in accordance with relevant ethical requirements (see paragraph A30); or
- (c) Law, regulation or relevant ethical requirements provide the auditor with the right to do so (see paragraph A31).

A29. In some jurisdictions, the auditor may be required by law, regulation or relevant ethical requirements to report identified or suspected non-compliance with laws and regulations to an appropriate authority outside the entity. For example, in some jurisdictions, statutory requirements exist for the auditor of a financial institution to report the occurrence, or suspected occurrence, of non-compliance with laws and regulations to a supervisory authority. Also, misstatements may arise from non-compliance with laws or regulations and, in some jurisdictions, the auditor may be required to report misstatements to an appropriate authority in cases where management or those charged with governance fail to take corrective action.

A30. In other cases, the relevant ethical requirements may require the auditor to determine whether reporting identified or suspected non-compliance with laws and regulations to an appropriate authority outside the entity is an appropriate action in the circumstances. For example, the IESBA Code requires the auditor to take steps to respond to identified or suspected non-compliance with laws and regulations and determine whether further action is needed, which may include reporting to an appropriate authority outside the entity.¹⁷ The IESBA Code explains that such reporting would not be considered a breach of the duty of confidentiality under the IESBA Code.¹⁸

A31. Even if law, regulation or relevant ethical requirements do not include requirements that address reporting identified or suspected non-compliance, they may provide the auditor with the right to report identified or suspected non-compliance to an appropriate authority outside the entity. For example, when auditing the financial statements of financial institutions, the auditor may have the right under law or regulation to discuss matters such as identified or suspected non-compliance with laws and regulations with a supervisory authority.

A32. In other circumstances, the reporting of identified or suspected non-compliance with laws and regulations to an appropriate authority outside the entity may be precluded by the auditor's duty of confidentiality under law, regulation or relevant ethical requirements.

¹⁷ See, for example, paragraphs 360.21 A1 and 360.25 A1–R360.27 of the IESBA Code.

¹⁸ See, for example, paragraphs R114.1–114.1 A1 and R360.26 of the IESBA Code.

- A33. The determination required by paragraph 29 may involve complex considerations and professional judgments. Accordingly the auditor may consider consulting internally (e.g., within the firm or a network firm) or on a confidential basis with a regulator or professional body (unless doing so is prohibited by law or regulation or would breach the duty of confidentiality). The auditor may also consider obtaining legal advice to understand the auditor's options and the professional or legal implications of taking any particular course of action.

Considerations Specific to Public Sector Entities

- A34. A public sector auditor may be obliged to report on identified or suspected non-compliance to the legislature or other governing body or to report them in the auditor's report.

Documentation (Ref: Para. 30)

- A35. The auditor's documentation of findings regarding identified or suspected non-compliance with laws and regulations may include, for example:
- Copies of records or documents.
 - Minutes of discussions held with management, those charged with governance or parties outside the entity.
- A36. Law, regulation or relevant ethical requirements may also set out additional documentation requirements regarding identified or suspected non-compliance with laws and regulations.¹⁹

¹⁹ See, for example, paragraph R360.28 of the IESBA Code.