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The HKICPA's Standard Setting Department welcomes your comments and feedback on this guidance, which should be sent to commentletters@hki CPA.org.hk.

Responsibilities for NOCLAR by professional accountants in business

Imagine you are an accountant of a manufacturing company. In preparing the annual financial statements for statutory and tax filing purposes, you are skeptical that a substantial amount of revenue is fictitious. You raise your concern with the finance director. He replies with a smile and remarks that it is not your job to judge or criticize the company's revenue. Instead, he requests that you prepare the financial statements according to the amounts shown on the company's ledger. As a member of the Institute, what course of action would you take?

Responding to Non-compliance with Laws and Regulations ("NOCLAR") is an ethics standard ("NOCLAR standard") for all professional accountants. It sets out a framework to guide their actions in the public interest when they become aware of an actual or suspected NOCLAR committed by a client or employer.

What is NOCLAR?

According to the [Code of Ethics for Professional Accountants](#) ("Code"), NOCLAR comprises acts of omission or commission, intentional or unintentional, which are contrary to the prevailing laws or regulations committed by a professional accountant's client or employing organization, including by those charged with governance ("TCWG"), management or others working for or under the direction of the client or employing organization.

Given the different roles and categories of professional accountants, the NOCLAR framework specifies a differential approach to responding to NOCLAR for the four broad categories of professional accountants:

- Auditors
- Other professional accountants in public practice ("PAPPs")
- Professional accountants in business ("PAIBs") who are in senior-level roles, e.g., directors, officers or senior employees with ability to make decisions about acquisition, deployment and control of entity's resources
- Other PAIBs



Who are PAIBs?

For purposes of the Code, a PAIB is a professional accountant working in areas such as commerce, industry, service, the public sector, education, the not-for-profit sector, or in regulatory or professional bodies, who might be an employee, contractor, partner, director (executive or non-executive), owner-manager or volunteer.

With regard to PAIBs, laws and regulations covered by the NOCLAR are:

- (a) those that directly affect the determination of material amounts and disclosures in the employing organization's financial statements; and
- (b) other laws and regulations that require compliance with which might be fundamental to the operating aspects of the employing organization's business, to its ability to continue its business, or to avoid material penalties.

Examples include laws and regulations that deal with fraud, corruption and bribery, money laundering, tax payments, financial products and services, environmental protection, and public health and safety. Personal misconduct unrelated to the business activities of the employing organization and non-compliance by parties other than those listed in (a) and (b) above are not in scope.

NOCLAR requirements for PAIBs are set out in Section 260 in Chapter A of the Code. As a result of the NOCLAR standard, PAIBs can no longer turn a blind eye or do nothing to the actual or suspected NOCLAR they are aware of.

The NOCLAR standard enables professional accountants to set aside the principle of confidentiality under the Code and report the suspected or actual NOCLAR to an appropriate authority, provided that it is in the public interest and not prohibited by relevant laws or regulations.¹

In addition, the NOCLAR standard requires greater responsibility from senior-level PAIBs to take action to respond to identified or suspected NOCLAR compared to other professional accountants. The NOCLAR framework places renewed emphasis on the role of senior-level PAIBs in promoting a culture of compliance with laws and regulations and prevention of NOCLAR within their organizations.

¹ Example clauses relating to professional accountants' NOCLAR obligations are published by [CPA Australia](#) and [The South African Institute of Chartered Accountants](#), which could be considered for inclusion in engagement letters or employment contracts to emphasize that the professional accountant(s) concerned are bound by relevant requirements to report NOCLAR they encounter at work or in the course of providing professional services. Where necessary, members of the Institute can tailor similar clauses according to applicable laws and regulations for inclusion in relevant engagement letters or employment contracts.



NOCLAR Response Framework for PAIBs

As set out in section 260 in Chapter A of the Code, PAIBs should apply the following steps when they become aware of actual or suspected NOCLAR.

Step 1: Obtaining an understanding of the matter
<ul style="list-style-type: none">- Evaluate the nature and the circumstances in which the NOCLAR has occurred or might occur- Understand and apply the relevant laws and regulations to the circumstances- Assess the potential consequences to the employing organization, investors, creditors, employees or the wider public- Apply knowledge and expertise, and exercise professional judgment
Step 2: Addressing the matter
<ul style="list-style-type: none">- Discuss the matter with the immediate superior or next higher level of authority, and communicate it with TCWG- Comply with applicable laws and regulations, e.g., report the non-compliance to an appropriate authority if required by other laws and regulations²- Rectify, remediate or mitigate the consequences- Reduce the risk of re-occurrence- Seek to deter the NOCLAR if it has not yet occurred- Determine whether disclosure to the employing organization's external auditor is needed
Step 3: Determining whether further action is needed
<ul style="list-style-type: none">- Assess the appropriateness of the response of the superiors and TCWG, if any- In light of that response, determine if further action is needed in the public interest by applying professional judgment and a reasonable and informed third party test²- Further actions may include informing the parent entity if applicable; disclosing the matter to an appropriate authority³; resigning from the employing organization
Step 4: Documentation
<ul style="list-style-type: none">- According to section 270. 27A1, PAIBs are encouraged, but not required, to document their consideration and actions to include:<ul style="list-style-type: none">▪ The matter▪ How management/ TCWG have responded to the matter▪ Course of action considered, judgments made and decisions taken▪ How responsibility to act in the public interest has been met

² For the purposes of the Code, the reasonable and informed third party test is a consideration by the professional accountant about whether the same conclusions would likely be reached by another party. Such consideration is made from the perspective of a reasonable and informed third party, who weighs all the relevant facts and circumstances that the accountant knows, or could reasonably be expected to know, at the time that the conclusions are made. The reasonable and informed third party does not need to be an accountant, but would possess the relevant knowledge and experience to understand and evaluate the appropriateness of the accountant's conclusions in an impartial manner.

³ Paragraphs 260.20 A1 to 260.20 A3 in Chapter A of the Code provide guidance to assist PAIBs' determination of whether to disclose the matter to an appropriate authority. PAIBs might also consider seeking advice in accordance with paragraph 260.19 A1 in Chapter A of the Code, for example, obtaining legal advice to understand the accountant's options and the professional or legal implications of taking any particular course of action.



In short, PAIBs should take appropriate action when they become aware of NOCLAR committed by management or others at their employing organization.

PAIBs should also be aware that auditors engaged by the management to provide professional services are obliged to apply the Code's requirements on identified or suspected NOCLAR commissioned by a client. This includes auditors' disclosure of the matter to an appropriate authority where required by laws and regulations. For example, *Cap. 41 Insurance Ordinance* requires auditors to report to the Insurance Authority in writing if they become aware of evidence that an insurer or a licensed insurance broker company fails to comply with relevant conditions in the specified ordinance or rules⁴.

NOCLAR Illustrative Examples for PAIBs

The following NOCLAR scenarios are adapted from the publications of Consultative Committee of Accountancy Bodies (CCBA) and International Federation of Accountants (IFAC). Following the steps in the NOCLAR response framework listed above, what course of action should a PAIB take in response to the dilemma encountered?

1. A large international manufacturing company has developed an AI tool to pre-screen candidates for job placements. However, the data being captured by the system is also being sold to a data broker without the knowledge or consent of the interviewees. This is not in compliance with the local jurisdiction's data protection laws.

Click [here](#) to learn the PAIB's NOCLAR responsibilities to the scenario.

2. The tax computation of a start-up company submitted to the tax authority last year contained an unintentional error. When the company becomes aware of the error, the finance director is concerned that the company is facing cash flow difficulties and the repayment of previous year's tax credit would cause the company to breach bank covenants, prompting investors to withdraw their financial support. Instead of rectifying the error with the tax authority immediately, the finance director plans to send a revised computation to the tax authority and repay the overclaimed amount once the company's cash flow position improves by the end of the year.

Refer to Case Study 7 [here](#) to learn the PAIB's NOCLAR responsibilities to the scenario.

⁴ Relevant guidance is provided in the Institute's [Practice Note 620.2 \(Revised\)](#), *Communication between the Auditor and the Insurance Authority*.



Implementation Support

The Institute's [Resource Centre for the Code](#) contains guidance and material to support members' understanding and implementation of the NOCLAR requirements. Among others, an [e-seminar](#) on NOCLAR discussing the scope of the requirements, response framework and impact to professional accountants is available for subscription.

Technical enquiries in relation to the application and interpretation of the Code, including the NOCLAR provisions, can be submitted to the Institute [online](#), which will be responded by the HKICPA staff according to the [Institute's policy](#).