FINANCIAL REPORTING COUNCIL OF NIGERIA

FRC Rule 14 – Non-Compliance with Laws and Regulations

Background

As part of our commitment to ensuring the integrity of financial reporting and safeguarding public interest, the Financial Reporting Council (FRC) is introducing Rule 14 to clarify and strengthen the responsibilities of external auditors when responding to non-compliance or suspected non-compliance with laws and regulations.

A distinguishing mark of the accountancy profession is its acceptance of the responsibility to act in the public interest. When responding to non-compliance or suspected non-compliance, the objectives of the professional accountant are:

(a) To comply with the principles of integrity and ethical professional behavior.

(b) To alert management or, where appropriate, those charged with governance of the client, to seek to:

- (i) enable them rectify, remediate or mitigate the consequences of the identified or suspected non-compliance; or
- (ii) prevent or deter the company from non-compliance where it has not yet occurred; and
- (iii) to take such further action as appropriate in the public interest.

The current International Auditing and Assurance Standards (ISA) 250 and International Code of Ethics for Professional Accountants (IESBA) require the External Auditor to identify noncompliance with laws and regulations that have a direct and material effect on the financial statements. These standards have few requirements related to the auditor's identification of noncompliance (which has an indirect effect on the financial statements).

Some sections of these standards guide the accountant in assessing the implications of the matter and the possible courses of action when responding to non-compliance or suspected non-compliance with:

(a) Laws and regulations generally recognized to have a direct effect on the determination of material amounts and disclosures in the client's financial statements; and

(b) Other laws and regulations that do not have a direct effect on the determination of the amounts and disclosures in the client's financial statements, but which compliance with, might be fundamental to the operating aspects of the client's business, its ability to continue its business, or to avoid material penalties.

Key Observations:

Our experience has indicated that laws and regulations considered to have indirect effects on the financial statements, such as anti-money laundering regulations and environmental regulations, among others, can lead to substantial fines and penalties if violated. Moreover, our outreach has also indicated that the distinction in dividing illegal acts into categories of those with direct effects and those with indirect effects on the financial statements has been a source of confusion to investors and auditors. The auditing standards have historically used the distinction to limit the auditors' responsibilities – such that the auditor need only perform certain audit procedures depending on the category.

The Rule

The Council believes that removing this distinction will improve the auditor's identification of a company's noncompliance with laws and regulations which could have a material effect on the financial statements, potentially resulting in the auditors conducting better risk assessments, and in turn, designing and implementing better responses to the identified risks of material misstatement due to noncompliance with laws and regulations, and, in doing so, better protect investors.

One of such instances is signing financial statements with invalid FRC registration number or where a reporting entity is having outstanding compliance issue as a result of an ongoing inspection and monitoring program. This renders such financial statements invalid and shall not be accepted by any regulatory agency of government in Nigeria.

Consequence upon the above, the Council hereby makes it mandatory for auditors to ensure that all relevant sections of the FRC Act 2011 (as amended, Regulations, Codes, Rules, Guidelines and Guidance currently in forced and as may be issued from time to time, with direct or indirect effects on the financial statements and operations of entities are complied with by their clients.

Specific Requirements for External Auditors

1. **Verification of Compliance:** External auditors shall ensure that their clients comply with all relevant sections of the FRC Act 2011 (as amended), Regulations, Codes, Rules Guidelines and Guidance currently in forced and as may be issued from time to time —whether these have direct or indirect effects on financial statements and operations.

2. **Confirmation Before Signing Audit Opinions:** Auditors shall confirm that the reporting entity and all signatories to the financial statements have fulfilled their statutory obligations to the FRC, as required by FRC Rules 1 & 2 and Sections 33, 41(2), 42(1), and 44(1) of the FRC Act 2011 (as amended). This confirmation shall be obtained by sending an email to the FRC via: rule14@frcnigeria.gov.ng

By requiring External Auditors to identify, communicate and ensure compliance with relevant FRC's Laws, Rules and Regulations, entities would be encouraged to take more timely remedial actions and thereby reduce investment risk caused by legal and regulatory penalties.

Implications for Non-Compliance

Any auditor that fails to confirm compliance before signing audit opinions contravenes this rule and shall be sanctioned in line with the Council's Operational Guidelines for Inspection and Monitoring of Auditors, Other Assurance Providers and Audit Committee Members 2020.

Effective Date:

This Rule becomes effective on 1st January 2025.

Signed

Management

22nd January 2025