



National Treasury

[Released to facilitate and enhance public consultation on the Auditing Professions Bill only]

COMPANIES ACT, 1973: PROPOSED AMENDMENTS TO FURTHER ENHANCE THE INTEGRITY AND INDEPENDENCE OF THE SOUTH AFRICAN AUDITING PROFESSION

SUMMARY

November 2004

1. Introduction

Certain amendments to the Companies Act are required in order to achieve the objectives of the draft Auditing Professions Bill ("the Bill"). This document contains a summary of the recommendations made to the Minister of Trade and Industry, which are currently under consideration.

In order to facilitate and enhance the Cabinet sanctioned public consultation process on the draft Auditing Professions Bill, it was deemed expedient to release this summary together with the draft Bill, specifically as the proposed amendments to the Companies Act aim to establish and maintain the independence of auditors in support of the Bill.

It is envisaged that the proposed Companies Act amendments will be submitted to Parliament concurrently with the Bill.

2. Proposed amendments to the Companies Act

2.1 General

The proposed amendments relate primarily to section 1 (Interpretation) and Chapter X (Auditors) of the Companies Act. The terms "registered auditor", "firm" and "IRBA" as used in this summary have the same meaning as in the Bill.

2.2 Only registered auditors to be appointed

It is proposed that no person may henceforth be appointed auditor of a company unless that person is a registered auditor in terms of the Bill.

This means that all audits of company accounts will in future be subject to the controls and safeguards of the Bill.

2.3 Audit committees

2.3.1 Obligation to appoint

It is proposed that the board of directors of every public interest company¹ must for each financial year appoint an audit committee consisting of not less than three independent non-executive directors.

A director is an independent non-executive director if (except as a director and member of the audit committee) the director:

- ▶ Does not receive any direct or indirect remuneration or other benefit from;
- ▶ Does not undertake any consultancy, advisory or other work for; and
- ▶ Is not directly or indirectly connected with;

the company or any subsidiary or parent of the company or, if the company is a member of a group, any other member of the group.

2.3.2 Functions and funding

An audit committee of a public interest company will have the following duties with respect to the financial year for which it is appointed:

- ▶ to nominate an auditor for appointment who, in the opinion of the audit committee, is independent² of the company;

¹ A "public interest company" is defined as a company that is not a limited purpose company.

A "limited purpose company" is defined as a private company that does not:

- (i) take deposits or loans from the public;
- (ii) offer its shares to the public; or
- (iii) act as a holding company in respect of a public interest company; and
- (iv) is not a subsidiary or associate of, or joint venture with a public interest company, that is authorized by unanimous consent of its members to operate as a limited purpose company for purposes of the Companies Act; provided that such consent is given annually in respect of each supervening financial year.

² In considering whether a registered auditor is independent of a company, the audit committee must determine if the auditor, in respect of services other than auditing or permitted non-audit services (see paragraph 3.3.6):

- (i) receives any remuneration or other direct or indirect benefit from;
- (ii) undertakes any consultancy, advisory or other work for; or
- (iii) is connected, directly or indirectly, with;

the company or any subsidiary or parent of the company or, if the company is a member of a group, any other member of the group.

Where a registered auditor has previously been appointed as auditor of the company, audit committee must consider whether the auditor's independence may have been prejudiced as a result of such an appointment.

- ▶ to determine the fees to be paid to the auditor and the auditor's terms of engagement;
- ▶ to ensure that the appointment of the auditor complies with the provisions of the Companies Act and the Bill;
- ▶ to determine the nature and extent of any non-audit services which the auditor may provide for the company;
- ▶ to insert a statement in the financial statements as to whether or not the audit committee is satisfied that the financial statements and any audit of them are in compliance with the provisions of any applicable law and that the auditor is independent of the company;
- ▶ to receive and deal appropriately with any complaints (whether from within or outside the company) relating either to the accounting practices of the company or to the content or auditing of its financial statements or to any related matter.

A public interest company may appoint an auditor other than one nominated by the audit committee. Where such an auditor is appointed the appointment is only valid if the audit committee certifies that, in its opinion, the proposed auditor is independent³ of the company and that it is satisfied that it can carry out its duties with respect to the proposed auditor.

The effect of this amendment is that the functions and duties of the board of directors with respect to the appointment, fees and terms of engagement of the auditor, are reduced.

A public interest company will be required to meet all expenses reasonably incurred by its audit committee including, if the audit committee considers it appropriate, the fees of any consultant or specialist engaged by the audit committee to assist it in the performance of any of its duties.

2.3.3 Filling of casual vacancies

Where a casual vacancy arises in the office of the auditor of a public interest company during the tenure of an audit committee the directors must within twenty days propose to the audit committee a registered auditor to become the new auditor.

2.3.4 Appointment of firm as auditor

The appointment of a firm as the auditor of a public interest company will be valid only if, in addition to the name of the firm, the appointment specifies the name of the individual registered auditor who is the member of the firm that will undertake the audit.

Where a change in the composition of the members of the appointed firm results in less than one half of the membership that existed at the time of the appointment remaining, such a change constitutes as a resignation of the auditor and a casual vacancy shall be taken to have arisen accordingly.

³ See footnote 2.

2.3.5 Rotation of auditors

The same individual may not serve as the nominated auditor of a public interest company for more than four consecutive financial years. Where an individual has served as the nominated auditor of a public interest company for two or more consecutive financial years and then ceases to be the nominated auditor, the individual may not again become the nominated auditor of that company until after the expiry of at least two further financial years.

2.3.6 Certain non-audit services not open to current auditor of public interest company

An individual that is the nominated auditor of a public interest company may not perform any book-keeping, accounting (as distinct from auditing) or internal audit services for that company.

Additional limitations on non-audit services are also proposed:

- ▶ The Minister may prescribe further services which an auditor may not perform for a public interest company during a financial year for which she is the nominated auditor.
- ▶ The audit committee may limit further the services which an auditor of a public interest company may perform; and
- ▶ A registered auditor may not conduct the audit of any financial statements of an entity (whether as an individual auditor or as a member of a firm) if, at any time during a period to which those financial statements relate or at any time during the two years ending at the beginning of that period the auditor has or had a financial interest in the entity (see section 21 of the Bill).

2.3.7 Resignation of auditor

An auditor intending to resign will be required to deliver to the company and to the Registrar a written notification (in the prescribed form) to the effect that he or she has no reason to believe that in the conduct of the affairs of the company a reportable irregularity, within the meaning of section 22 of the Auditing Profession Bill has taken place or is taking place which has caused or is likely to cause financial loss to the company or to any of its members or creditors, other than an irregularity (if any) which has been reported to IRBA under that Act.

2.3.8 Attendance of certain meeting by auditors

Public interest company: The appointed auditor will be required to attend a meeting of the board (which meeting may not take place more than one month before the date of the annual general meeting at which the financial statements of the company for any financial year are to be considered) to consider with the board matters which appear to the auditor or the board to be of importance and relevant to the proposed financial statements and to the affairs of the company generally.

The appointed auditor must attend every annual general meeting at which the financial statements of the company for a financial year are to be considered or agreed, and respond to the best of his or her ability to any question which is put to his or her and is relevant to the audit of the financial statements.

Limited purpose company: Where due notice is given of the intention to move a resolution requiring the presence of the auditor at an annual general meeting of the company at which financial statements of the company for any financial year are to be considered, the auditor will be required to attend that meeting and respond to the best of his or her ability to any question which is put to him or her and is relevant to the audit of the financial statements.

Failure to attend the above-mentioned meetings is an offence unless the nominated auditor:

- ▶ is prevented by circumstances beyond his or her control from attending the meeting;
- ▶ the auditor ensures that another individual who is a registered auditor attends the meeting in place of the nominated auditor and carries out the duties of the nominated auditor at the meeting; and
- ▶ in the case of a public interest company and if the nominated auditor is a member of a firm, the individual attending the meeting in place of the nominated auditor is a member of that firm.

