



SizweNtsaluba VSP

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Draft Auditing Profession's Bill, 2004

It is our pleasure to submit our views on Draft Auditing Profession's Bill. We hope that our comments will contribute towards creating a sound Act to govern the auditing profession in order to support the objectives of society at large as well as member's of the profession.

Discussion on the Draft Bill

Composition of the Independent Regulatory Board for Auditors

- ❑ Bill must refer to Minister's consideration of transformation, gender equality, and diversity issues in his selection of the members of the IRBA, in particular relating to members selected from amongst registered auditors
- ❑ In addition to the 4 registered auditors the Auditor General should also be included as a member of the IRBA, as well as another person with a background in the profession but who is no longer a practising registered auditor
- ❑ An representative of Tertiary Learning Institutes should also be included as a member of the IRBA, particularly a person representing previously black dominated universities
- ❑ The remaining positions may be filled at the Minister's discretion with due consideration for the objectives of the IRBA.
- ❑ As a general comment we do believe that it is in the interest of the public that the majority of persons appointed to the IRBA should be knowledgeable about the auditing profession, whilst taking due note for the need for independence and accountability on a wider scale. The inclusion of retired audit professionals or those no longer actively engaged in the profession would go a long way towards ensuring that the effectiveness of the IRBA is not compromised whilst maintaining its independence.

Objectives of the IRBA

- ❑ Objectives of the IRBA should include as specific and separate objectives points relating to transformation of the profession and gender equality

IRBA Powers and Duties

- ❑ Section 5 (1)(e) refers to the IRBA's powers to determine the need, nature and level of indemnity or fidelity insurance to be carried by a registered auditor. SizweNtsaluba VSP is of the view that due consideration of the impact of this on black accountants should be made, so that this does not become a barrier to entry into the profession. Furthermore it is noted that should one not carry sufficient amounts of professional insurance covers, one could expose personal assets in the event of a successful and this may also act as a disincentive for prospective black students to enter the professional. Whilst SizweNtsaluba VSP acknowledges that it does not have any specific recommendations on this matter at this time, it calls for more discussions to be held to identify a solution that is fair and equitable.
- ❑ We believe that it is necessary to review the philosophy around the unlimited liability of auditors with a view to bringing South Africa in line with global trends around the limitation of such possible claims. A balance needs to be struck between the interests of the public as well as the interests of auditors who by and large conduct their affairs with due competence and in good faith.
- ❑ Section 5(5) refers to the limitation of the IRBA's power to overrule the decisions of some of its committees. SizweNtsaluba VSP is of the view that this removes accountability from the IRBA, which is ultimately answerable to the Minister for all actions undertaken in its name. SizweNtsaluba VSP is of the view that no such limits on the IRBA's power should be allowed, and that the IRBA should exercise its discretion on such matters.

Accreditation

- ❑ We believe that in the public interest the final Act should itself prescribe with a reasonable degree of detail the minimum standards required for accreditation and not delegate in full the entire process to the organs contemplated in this draft bill.
- ❑ We would anticipate that one such minimum standard would be to pass a common exam set by the IRBA, or the relevant sub-entity of the IRBA, which would encompass the examination of technical competence as well as the practical application of technical knowledge.
- ❑ Whatever the level of detail that is finally inserted into the Act, the Act itself should seek to maintain the high standards of technical competence and ethical practices that the profession in South Africa enjoys. As part of a global environment where foreign capital participates in our daily economic activities, we believe it is essential that we retain the confidence that investors have in the quality of work performed by South African auditors.

Termination of accreditation of member

- ❑ Section 10(2)(c) allows for the cancellation of the registration of a registered auditor who ceases to be a member of an accredited professional body, albeit allowing for 21 days in which the member may submit grounds for not proceeding with cancellation. SizweNtsaluba VSP is of the view that more protection should be included for registered auditors who may feel that they have been discriminated against in their respective professional body on the basis of gender or race or any other unfair basis. Rights of appeal and or arbitration processes should be included in the draft bill to ensure that individual members rights are not disregarded.

Functions and Composition of Subsidiary Boards

Registration of auditing firms

- ❑ The draft bill is silent on the issue of multidisciplinary practices (most medium and large audit firms would fit into this category), and in particular fee sharing with Non-registered auditors. We believe the Act in its final form should address this in sufficient detail.

Standard-Setting Board for Auditor Ethics (SBE): composition

- ❑ Bill must refer to the IRBA's consideration of transformation, gender equality, and diversity issues in its selection of the members of the SBE, in particular relating to members selected from amongst registered auditors
- ❑ At least one of the 5 registered auditors on the SBE should be one of the registered auditors included on the IRBA. This will ensure a smooth flow of information between the bodies and the effectiveness of both bodies. This individual may take the role of Chairperson.

SBE Powers and Duties

- ❑ A clear line of reporting, responsibility, and overall accountability must be established between the IRBA and the SBE
- ❑ SizweNtsaluba VSP feels that before the SBE sets any rules or regulations of a substantive and non-administrative nature such rules and regulations must first be tabled before and approved by the IRBA.

Standard-Setting Board for Auditing (SBA): composition

- ❑ Bill must refer to the IRBA's consideration of transformation, gender equality, and diversity issues in its selection of the members of the SBA, in particular relating to members selected from amongst registered auditors
- ❑ At least one of the 5 registered auditors on the SBA should be one of the registered auditors included on the IRBA. This will ensure a smooth flow of information between the bodies and the effectiveness of both bodies. This individual may take the role of Chairperson.
- ❑ Notwithstanding our recommendation that the Auditor General be given a seat on the IRBA, SizweNtsaluba VSP feels that a senior representative of the Auditor General's office be included on the SBA
- ❑ In order to balance our recommendation that a representative of previously black dominated universities sit on the IRBA, we believe that a representative of previously white dominated universities sit on the SBA
- ❑ We believe that the banking industry may also be over-represented by including representatives of the Financial Services Board as well as the Registrar of Banks. We

believe that a representative of the Johannesburg Securities Exchange (JSE) should substitute one of these representatives.

SBE Powers and Duties

- ❑ A clear line of reporting, responsibility, and overall accountability must be established between the IRBA and the SBA
- ❑ SizweNtsaluba VSP feels that before the SBA sets any rules or regulations of a substantive and non-administrative nature such rules and regulations must first be tabled before and approved by the IRBA.

General Obligation of Registered Auditors in relation to Audit

- ❑ Reference to South African Auditing Standards should be augmented by reference to International Standards on Auditing
- ❑ References to the work conducted by and auditor should use the term “material” as the purpose of an audit is not to give absolute assurances. The terms used in this section are appropriate for a company’s obligations in relation to its own financial statements but are unrealistic with reference to the conduct of an audit as the level of assurance given is based on issues with take regard of the materiality of transactions. Section 2 of Chapter IV should be amended to reflect this reality.

Auditor having a financial interest in entity excluded from audit

- ❑ We believe that references to financial interest should be qualified to “material financial interest”, in the context of the firm and or an individual auditor in his personal capacity or as part of a firm of auditors.

Auditor’s report on irregularities

- ❑ We believe that the requirement to report without first following a process to alert audit clients of the issue of concern could lead to a break-down in the relationship between auditor and client. We believe it is only appropriate to report irregularities to the IRBA when a due process has been followed and the client has been informed of the concerns and given a reasonable opportunity to respond.
- ❑ The concession that the IRBA will not disclose the name of the auditor who reports an issue under this section to the regulatory body of the client concerned is of questionable benefit because the client and the regulatory body are able to trace whom the auditor is as this is a matter of public record. We believe this will ultimately expose the auditor and will not be an effective protection as intended.

Limitation of liability for auditor for opinions, reports, statements, etc

- ❑ We believe the term “client” needs to be specifically defined as intended in this section.

Disciplinary Matters

Composition of Disciplinary Tribunal

- ❑ Bill must refer to the IRBA's consideration of transformation, gender equality, and diversity issues in its selection of the members of the Disciplinary Tribunal, in particular the Tribunal President
- ❑ The draft bill must include a minimum number of members that constitute the DT, and SizweNtsaluba VSP recommends a minimum of no less than 5 members.

Composition of Disciplinary and Investigation Committees

- ❑ Bill must refer to the IRBA's consideration of transformation, gender equality, and diversity issues in its selection of the members of disciplinary and investigation committees
- ❑ The draft bill must include a minimum number of members that constitute a disciplinary or investigation committee. SizweNtsaluba VSP recommends a minimum of 3 members for an investigation committee and 5 members for a disciplinary committee

Evidential Provisions applicable to Investigations and hearings AND Disciplinary Hearings

- ❑ Section 29(2) states that evidence given for the purpose of any investigation or hearing nor any decision on a hearing may be used by or against a person whose conduct is the subject of the investigation or hearing in any subsequent civil or criminal proceeding in any court, but may be used in disciplinary proceedings before any professional body.
- ❑ Section 30(5) states that a hearing before a disciplinary body is open to the public except where, in the opinion of the Tribunal President, or as the case may require, the chairperson of a disciplinary committee, any part of the hearing should be held in camera.
- ❑ SizweNtsaluba VSP feels that the 2 sections above are potentially in conflict with one another as a public hearing may result in criminal and or civil proceedings against the subject of the hearing, notwithstanding the provisions of section 29(2).
- ❑ Irrespective of the potential legal conflict between the above sections, SizweNtsaluba VSP feels that the outcome of disciplinary hearings where a verdict of guilty has been arrived at should however be publicised appropriately.

Lack of Appeals Process

- ❑ The draft bill lacks the outline of an appeals process by registered auditors that are dissatisfied with the outcome and or conduct of investigations or disciplinary hearings. There needs to be a clear appeals process outlined in the bill to protect the rights of registered auditors.

Committees

Section 42(4) deals with the ability of the IRBA to assign and regulate powers of its committees. SizweNtsaluba VSP disagrees that the IRBA, as part of the appeals process referred to above

should not have the power to review and overrule the decisions of its committees and subsidiary boards, SBE and SBA.

General Comments

- We are concerned that the only source of funding for the activities of the IRBA and its sub-organs will be from registered auditors. We believe that in the interests of reducing the risk of the IRBA's objectives being compromised due to a disproportionate financial dependency on the very firms and individuals it is suppose to regulate, the sources of funding should be broadened to include other sources such as the national fiscus, as an example. Experience has shown that money is usually accompanied by power and influence and the final Act should take cognisance of that.

Proposed Amendments to the Companies Act, 1973

Rotation of auditors

- SizweNtsaluba VSP is of the view that the basis of auditor rotation to be broadened to include the rotation of firms and not merely individual auditors within the same firm. The basis of this view is that many discussions in the past have identified the rotation of audit firms as being a possible way of increasing the participation of black audit firms in the audits of predominantly white entities.
- SizweNtsaluba VSP feels that audit firms should be rotated on a 5-year cycle, with due consideration for circumstances where black firms are the incumbent auditors and considerations of transformation may be used to elongate the period before rotation.
- We also believe 5 years is a reasonable for an auditor to develop an adequate understanding of his client's business activities as well as allowing for it to remain a commercially worthwhile undertaking to invest in knowledge and technology to improve audit quality and effectiveness.
- Partnering of black audit firms with traditionally white audit firms in industries where special or unique expertise, e.g. financial services and mining, should also be investigated to broaden the participation of black audit firms in these industries. Due consideration of these relationships should be made when applying the rules of rotation

Participation of auditors at AGM's

- We are concerned that the proposal that auditors be required to answer questions at client's Annual General Meeting will result in "scope creeping". By this we mean that the auditors report and opinion are sufficient to express all the pertinent matters relating to the conduct of an audit, should there be question relating to the financial statements the Director's should be responsible for responding to them. It is must be remembered that in the litigious environment in which we are now operating comments made at the AGM could arise in claims against the auditor especially considering the there would be no opportunity to filter the response to the normal quality control and risk management procedures that the audit report has been subjected to.
- We propose that this requirement be removed or amended to reflect that the auditor may only asked questions relating to the audit report itself. Alternatively the Act should

indemnify auditors for claims that may result out of comments made at AGM's on the basis that there is likely to be insufficient time to quality check the responses given.

OVERRULING OF THE AUDIT COMMITTEE

- From the draft amendments it isn't clear who has the power to overrule the choice of the audit committee with respect to appointing auditors. We are concerned that this may lead to the loss of effectiveness and independence of the audit committee. Our proposal is that should it be possible to overrule the audit committee's choice, this power be reserved only for shareholders.

Conclusion

We hope our contribution will prove useful in shaping the manner in which the profession conducts its affairs in the interest of all affected parties.

SizweNtsaluba vSP Inc.

Date: _____