

Tel 021 406 3598
Fax 021 406 3366
e-mail fgroepe@media24.com

P O Box 579
Kuils River
7579

10 February 2005

Auditing Professions Bill
Director : Local Government Implementation Office 1809
Private Bag X115
PRETORIA
0001

Dear Sir/Madam

COMMENT ON THE DRAFT AUDITING PROFESSIONS BILL, 2004

I wish to thank you for the opportunity to comment on the Draft Auditing Professions Bill, 2004.

There is general consensus that the auditing professions' responsibility is to protect the public interest. It is therefore of cardinal importance that it acts both independently and in a transparent fashion. In pursuance of these objectives, it is proposed that consideration being lent to the following proposals:

- i) That auditing firms be restricted with regard to the provision of non-audit services to their clients. This is consistent with the latest international trends, notably in the USA and will serve to further improve auditor independence.

I have had experience of implementing such a regime within a big public corporation, and believe that it can work well in practice.

- ii) That audit firms be rotated every 10 years, i.e that rotation goes beyond mere rotation of partners. The length of the period will ensure that negative cost implications (if any) will be less pronounced – it may even contribute towards keeping fee escalations in check as most firms would probably call for tenders at the time of rotation. It is furthermore argued that the potential benefits will outweigh the negatives that may arise from such a practice.

What however needs to be borne in mind is the risk that at the time of rotation that staff switch from the auditee, to the audit firm that has won the tender at the time of rotation, as has been the case recently in particularly Italy.

- iii) The public's confidence in the auditing profession would be further boosted if the auditing firms lead by example by being more transparent and by them demonstrating a correct and acceptable interpretation and implementation of the very same accounting and auditing standards that they are meant to uphold, implement and regulate. It is argued that this will serve to strengthen auditing firms' moral authority and arguably improve the public's confidence in the broader profession.

The irony of the current situation is that those that are entrusted to protect the public's interest are falling significantly short on many areas of corporate governance - from deficiencies in respect of board composition, to lack of auditing committees, and possibly non-compliance with GAAP.

It is conceded that currently such a legal duty does not exist. It is however argued in the public interest that this is justified – the profession's influence is for example often much wider than many appreciate. By way of example: the adoption of AC116 has had two significant implications on the broader South African socio-economic landscape, namely the phasing out of defined benefit pension schemes, and the subsequent implementation of defined contribution schemes. This has resulted in the shifting of investment risks to employees and will significantly increase the burden on the public social security net in the future. The adoption of AC116 has furthermore contributed towards the phasing-out of medical aid subsidies to employees by employers in order to reduce or eliminate post-retirement medical aid liabilities on company balance sheets.

Admittedly it would be wrong to blame the (local) auditing profession for the above consequences, but what the example attempts to demonstrate is that accounting and/or auditing rules often impacts more widely than is commonly held.

It is worth pointing out that the industry is dominated by a few large players in a situation that reminds of an oligopoly. The question that is rightfully being begged is whether the call for greater transparency and disclosure is not fully justified against the backdrop of the circumstances sketched above.

In summary therefore it is proposed:

- a. that auditing firms with a turnover of say more than R100m p.a be required to publicly disclose their audited financial statements;
- b. that they be required to appoint a Board of Directors, with a majority of independent directors, and
- c. that they be required to appoint Board sub-committees in accordance with good corporate governance practice.

The benefits are - greater transparency; it will inspire greater public confidence in the sense that one would gauge whether these firms maintain the high standards

they serve to maintain and enforce and it will eventually put downward pressure on auditing fees.

In conclusion, the draft bill will go some way to improve governance, but there remain room for further improvements.

Qualification: I have written the letter in my personal capacity, and the opinions and views expressed are solely mine, and in no way reflect views and opinion of any of the organizations that I am involved with.

Yours faithfully

FRANCOIS GROEPE Hons B.Com, MBA, PG Dip Tax, Chartered Management Accountant