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8 February 2019

Ms Teboho Sepanya

Per email: (tsepanya@parliament.gov.za)

Dear Madam,

Submission of Commentary and Recommendations on Proposed Amendments to the Auditing Professions Act, Act 26 of 2005.

In response to the request for written representations to be made on the proposed amendments to the Auditing Professions Act, Act 26 of 2005 ("APA") we hereby present our submission for your consideration.

We welcome the publication of the second reading of the draft amendments to the APA for public comment.

We respectfully express our concern however about the short period allowed for members of the public to consider and comment on the proposed amendments. We believe the period is insufficient to allow the professionals and other stakeholders affected by this legislation to fully consider the specific wording and their impact. We note that the inclusion of the "Powers to enter and search premises" and the related "Warrants" sections, require significant consideration by stakeholders. We would have hoped to be able to perform more research in respect of how other jurisdictions have handled similar provisions and/or whether or not there are even such powers granted to an audit regulator however the lack of time given has prevented us from doing so.

We support the goal of the legislature to enable the Independent Regulatory Board for Auditors ("IRBA") to have the powers to respond more quickly or efficiently in the context of investigations and disciplinary matters. We, however, believe that an increased agility to act should not come at the expense of any actual or perceived reduction in a fair and just process, as this may ultimately result in the processes being stifled by subsequent legal challenges.

While there are many aspects in the draft amendments that we fully support, there are various matters that we believe should be reconsidered or amended to more effectively achieve the stated objectives of the legislation.

We thank you for the opportunity to provide comment on suggested amendments to the APA. Should you wish to discuss any of the comments with us, please contact Roger Hillen (011 772 3522), Michael Bourne (021 443 0258) or Michael Schafer (011 772 5400).

Yours faithfully

Roger Hillen

Professional Practice Director

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Detailed Comments on Proposed Amendments to APA

The section references below in our headings refer to the sections of the Auditing Professions Act, 26 of 2005 ("APA") proposed to be amended by the Financial Matters Amendment Bill [B 1 – 2019] ("the Bill").

Section 11 – Appointment of Members of the Regulatory Board

We note that the amendments to section 11 of the APA require that the Minister to appoint competent persons who are independent of the auditing profession. The amendment does not, however, include specific criteria against which the independence of the prospective members is to be assessed. In the absence of such criteria, or a statement that the independence of the prospective board member will be determined solely without the right of challenge (and on an ongoing basis) by the Independent Regulatory Board for Auditors ("IRBA"), we believe that the IRBA opens itself for challenge upon the outcome of any disciplinary or resolutions taken by the IRBA Board.

We therefore recommend that section 11 place the obligation of the final determination of the independence of the members on the IRBA itself.

In doing so we believe that the mere receipt of retirement benefits from a firm or an associated fund of the firm should not in any way be a factor in considering the independence of an individual from the auditing profession. This should in our opinion be specifically mentioned in the Act.

We welcome the amended in section 11(2A) which requires that the board include at least one person who was a registered auditor and has at least 10 years' experience in auditing. We recommend that experience in auditing be amended to require "at least 10 years' experience as an 'attest' audit partner". This recommendation is also considered relevant to section 17A(3)(a).

We also take this opportunity to recommend an amendment to section 15(4). Our recommendation is that the quorum requirement for each meeting should be such that at least one of the two individuals with the qualities referred to in section 11(2A)(a) and (b) should be at each meeting to ensure that a registered auditor's and legal adviser's knowledge and experience will be brought to bear on decisions of the Board.

Section 17A – Subcommittees of Regulatory Board

We welcome the requirement for the enforcement committee to include at least one (previously) registered auditor as well as an experienced attorney/advocate. We do however note, that whilst section 11(6) makes allowances for an alternate member, section 17A does not. It is not clear if it is the intention that should either of these members be unable to fulfil their duties in relation to the enforcement committee, that an alternative, who is similarly qualified and experienced, will be required to take their place. We propose that section 17A be further amended to include such a requirement:

> *17A(3)(c) Where the either of the members referred in in (a) or (b) is unable to fulfil their duties in relation to the enforcement committee, an alternative who is similarly qualified is required to take their place.*

As section 24C introduces some commonality of members between the disciplinary committee and the disciplinary panel, we recommend that the enforcement committee and the investigating committee also share some commonality but remain wholly separated from the disciplinary committee and panel. Our view is based on the following;

- The amendments have introduced several committees and panels which without such commonality of membership may cause the process to be slow and ineffectual.
- We believe that separation of the committees which investigate and enforce sanctions and the committees responsible for the hearings and recommendation of sanctions is crucial to ensuring a fair process.

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Section 24A – Powers to Enter, Search Premises, and Summarily Seize Documents and 24B - Warrants

Clause 20 of the Bill proposes insertions of sections 24A to 24C into the APA. The addition of these sections allows for the investigating committee to authorise a representative from the IRBA to enter any premises without prior consent or notice, if accompanied by a warrant (section 24A(1)(c)), or without notice if permission is granted (section 24A(1)(a)).

In every other respect the Audit Professions Act and the IRBA treat the auditing profession as a body of professionals held to abide by a strict code of professional conduct and professional ethics. The insertions of these sanctions appear in opposition to how the audit profession is viewed elsewhere in the Act. We do not believe that sufficient cause has been given which makes it necessary for the IRBA to have such significant powers of search and seizure. Whilst some may argue that there has been a breakdown of trust, from both sides, between the IRBA and the profession; these amendments are neither likely to restore that trust nor cause there to be a built a relationship of mutual respect which is established with rules for fair play. While we concede that the IRBA does require some mechanisms for enforcing its regulations on registered auditors, the granting of these powers to a regulator, as currently provided for in the Bill, is thought to be extreme.

We note that at present the IRBA has the right to inspect documents and evidence relating to audit files as part of their inspections process. Section 54(2) makes is an offence where a registered auditor does not comply with information requests relating to inspections under section 47(3). We are also unaware of any auditors who have not been complying with such requests. It is in this context that we believe that these provisions should only be required for exceptional circumstances when the IRBA have exhausted all the less intrusive powers in the APA which are already extensive in relation to obtaining documentation from auditors.

We note our specific concerns and suggestions below:

We would recommend that sections 24A to 24C be removed in their entirety from the Bill. This is because a warrant to search the premises of the accused is normally a last resort to obtain evidence in a civil or criminal matter. The amendment makes it that the IRBA simply approach a Judge or Magistrate to obtain a warrant and can, effectively, embark on a "fishing exercise" throughout an entire company. This raises numerous concerns, namely:

- This provision is contrary to the Protection of Personal Information Act 4 of 2003 ("POPI"), which requires the processors of personal information to protect such information and to obtain consent of the data subject in the event their personal information needs to be shared.
- This provision grants the IRBA powers of entry and search greater than that of the South African Police Service ("SAPS"). The SAPS are granted entry and search powers in terms of Chapter 2 of the Criminal Procedure Act 51 of 1977 ("the CPA"). At section 25, the CPA sets out the power of SAPS to enter premises in relation to "State security or any offence" i.e. there must be reasonable grounds that an offence has been committed, or is likely to be committed for a warrant to be granted. Police simply cannot enter premises because an investigation is being conducted by the State, they have a stringent set of criteria they need to adhere to and which must be proven if a warrant is required. The rationale for such stringency is to protect the individual's right to privacy in terms of section 14 of the Constitution of the Republic of South Africa ("the Constitution").
    - In granting a warrant to the SAPS the Courts must consider:
        - *"that the internal security of the Republic or the maintenance of law and order is likely to be endangered by or in consequence of any meeting which is being held or is to be held in or upon any premises within his area of jurisdiction; or (b) that*

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an offence has been or is being or is likely to be committed or that preparations or arrangements for the commission of any offence are being or are likely to be made in or upon any premises within his area of jurisdiction," (section 25 of the CPA).

- Section 25 of the CPA sets out how serious the situation must be for a Court to grant a warrant to enter and search the premises. Most notably, the "*internal security of the Republic or the maintenance of law and order is likely to be endangered*" or "*that an offence has been or is being or is likely to be committed*". It is important to note that "offences" are set out in schedules to the CPA giving the Court clear direction.

- In contrast, should sections 24A to 24 C be enacted into legislation, the Courts when considering the granting of a warrant for the IRBA to enter and search, simply have to determine (1) that an investigation is ongoing (proposed section 24A(1)); (2) a contravention of the APA – no matter how insignificant – has occurred, is occurring, or may occur (proposed section 24B(1)(b)(ii)(aa)); and (3) such entry may result in some information pertaining to such contravention (proposed section 24B(1)(b)(ii)(bb).

- Points (1) through (3) above are a far cry affecting the "*internal security of the Republic*" or *"the maintenance of law and order"*. The Courts will also not have to consider the severity of the contravention of the APA – as they would consider the severity of the crime under the CPA with assistance from the aforementioned schedules.

- In the event of a financial crime, however, the provisions of the CPA may be used to obtain a warrant to enter and search premises. Once again, noting the severity of the offence (or alleged offence) which is required to impeded on the Constitutional right to privacy.

We, therefore, recommend that the rights of entry and search are removed in their entirety from the Bill, as if they are carried through into law, as they are currently written, they will grant a regulatory body for auditors more power than the SAPS.

We would recommend, as an alternative to the current entry and search provisions, that the APA be amended to provide timelines to which detailed responses to requests for information from the IRBA (or the relevant investigating body) must be received. We would even understand and recognize the imposition of pecuniary fines in the event such deadlines are missed, or the information received is clearly to placate the IRBA and not to assist with the investigation.

In the event Parliament concludes that search and seizure powers should be granted to the IRBA then, in our view, the APA should provide for other avenues before the IRBA are able to obtain a warrant. The provisions should require a Court to consider the grant of a warrant on a balance of convenience i.e. a warrant may only be granted if the Judge is satisfied that IRBA has explored all other reasonable steps to obtain the documentation and information that they require for their work

In our view, "reasonable steps", in order of precedence, would be:

- Obtaining information, working papers, and other documentation through the inspections process in section 47.

- Obtaining information, working papers and other documentation through the subpoena process envisioned in section 48(5)(a)(i).

- Formal written requests for information, working papers, and other documentation. Such requests should include reasonable timelines in which this must be provided. Requests should provide the registered auditor with appropriate description of what is required.

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- Where outside of the inspections process, making formal written requests to visit the premises of the registered auditor to obtain information, working papers, and other documentation, to which consent may be given or denied by the registered auditor. Requests should include the name of the audit client and audit partner, as well as the financial year to which the request relates.

Search and seizure rights should only be granted when all other avenues have failed and the IRBA has provided substantiation thereof. The amendments to the APA should also guide the Court as to what is required in the warrant and its specificities in respect of the documentation the IRBA expects to find. Further the warrant should include specifics such as, the audit client, the audit partner, and the financial year end.

The APA amendments do not give the firm or registered auditor the right to be represented by legal counsel or adviser during a search and seizure intervention. We believe the APA should give that right to the firm and registered auditor concerned. This will also require that adequate notice be given to the registered auditor prior to any search or seizure action.

In addition, the APA should allow the firm or registered auditor a reasonable opportunity to make copies of any document or electronic documentation if the IRBA representative wishes to remove the same from the offices of the firm or registered auditor.

Section 24A(6): We note that there is some inconsistency in the language used in section 24A(6)(a); it is not clear if these are deliberately intended to convey a separate meaning or not. Specifically, where 6(a)(iii) and 6(a)(iv) require that information be "relevant to the investigation", 6(a)(i) and 6(a)(vii) require that information/evidence be "relevant to the request". Further, 6(a)(ii) and 6(a)(v) contain no requirement for the information/evidence/request be relevant to either the investigation or the request. We therefore recommend that the wording in these sections be updated to be consistent. The following suggestion is made:

> *(6) (a) While on the premises in terms of this section, the official, for the purpose of conducting the investigation, has the right of access to any part of the premises and to any document or item on the premises, and may do any of the following:*
>
> > *(i) Open or cause to be opened any strongroom, safe, cabinet or other container in which the official reasonably suspects there is a document or item that may afford evidence of the contravention concerned or be relevant to the ~~request~~ investigation;*
> >
> > *(ii) examine, make extracts from and copy any document on the premises which is relevant to the investigation;*
> >
> > *(iii) question any person on the premises to find out information relevant to the investigation;*
> >
> > *(iv) require a person on the premises to produce to the official any document or item that is relevant to the investigation and is in the possession or under the control of the person;*
> >
> > *(v) require a person on the premises to operate any computer or similar system on or available through the premises which is relevant to the investigation to—*
> >
> > > *(aa) search any information in or available through that system; and*
> > >
> > > *(bb) produce a record of that information in any media that the official reasonably requires;*
> >
> > *(vi) if it is not practicable or appropriate to make a requirement in terms of subparagraph (v), operate any computer or similar system on or available through the premises which is relevant to the investigation for a purpose set out in that subparagraph; and*

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(vii) take possession of, and take from the premises, a document or item that may afford /evidence of the contravention concerned or be relevant to the ~~request~~ investigation.

We also note our concerns in respect of the determination of what may be relevant to the investigation. This determination appears to be left at the discretion of "the official" conducting the search. The provisions of section 6(a) give free license for the official to search the entire premises, without objection, on the basis that something *may* contain evidence which *may*, in their determination, be relevant. This appears to confer significant powers of judgment on the official. Further, there is no indication of the qualification or experience of this official who will be making important determinations regarding relevance of information.

We note that this should be considered in the context that audit firms have significant amounts of confidential information for thousands of clients and client personnel which may not be related to the matter in question.

Furthermore, audit firms usually share premises with their advisory partners (who usually trade under co-branding) and who may also have their own confidential information not owned by or related to the audit statutory entity and which would be outside the jurisdiction of the IRBA.

Section 24B provides the Regulatory Board the mechanism to obtain a warrant for the purposes of the "Powers to enter and search premises" provisions. We note that in our comments above relating to section 24A we recommended that this provision be removed for the reasons noted above. Alternatively, section 24B should be amended to provide more specific conditions on requiring processes to be exhausted before obtaining a warrant and for the warrant to be more specific in relation to the matter being investigated.

Should this section remain we do not believe that a Magistrate should be able to grant such a warrant. Due to the fact that a Constitutional right is being impinged a Magistrate would in our view lack the jurisdiction for to grant such an order. Consequently, we recommend that the Bill should require that the application for a warrant to a High Court. We also believe that the APA should otherwise provide specific conditions on what should be considered before a warrant should be issued. Such considerations should (to mirror the CPA mentioned above) take into account the severity of the alleged offence and the prejudice which may be suffered in the event a warrant is not granted,

24B(b)(ii)(aa) refers to the fact that a warrant may be obtained for a contravention of the APA which includes any non-compliance with the auditing pronouncements (as defined in section 1). This casts a very wide net effectively giving the IRBA license to operate under an "enter and search premises" order for any perceived or actual contravention of either the Code of Professional Conduct for Registered Auditors, the International Standards on Auditing, or other sections of the APA itself without regard for whether such contraventions are material or trivial. We recommend, that should these sections not be removed, that "contravention with this Act" be qualified to refer to only material contraventions of the Act.

Section 45 – Duty to report irregularities

We welcome changes being made to section 45 which strengthen the position of the auditor when taking the right actions under the law.

Whilst we would like to see additional changes being made to section 45 which will make it easier for an auditor to report appropriate matters to the IRBA, we have not further repeated any of our detailed comments in this letter. We do however believe that there needs to be a re-evaluation of the section 45 provisions and the definition of a reportable irregularity.

We welcome the fact that the changes to section 45 provide protection to the auditor from being removed as auditor whilst the reporting process is ongoing. The amendment has made a distinction between the individual registered auditor and the registered auditor. This is understood to mean that neither the individual "audit partner" nor the "audit firm" may be *removed* until they have complied with section 45(3). Where the amendment creates uncertainty is, in our reading of the amendment the term "removed" or "remove" does not include an action taken by the registered auditor (i.e. resignation). The latest

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amendments appear to allow for the auditor to resign from the engagement prior to completion of reporting in terms of section 45.

We are, however, unsure that this was the intention in making this amendment and recommend that this section should clarify that the auditor can resign, before they are able to determine their response to the second letter.

Section 50 – Disciplinary Hearing

Clause 24 of the Bill further looks to amend section 50 of the APA and align it to the proposed revisions of section 49. On the whole we support this amendment and move away from the first reading, as now an accused has the right to an attorney; be heard; call witnesses; cross-examine witnesses and have access to the evidence against them (proposed section 50(9)).

Relating to the powers of subpoena we note that there is some inconsistency between the amendments to section 48(5)(a)(i) and section 50(4). Where the former allows for subpoena of only persons "with specific knowledge of the matter under investigation", the latter does not. If this was intentional, we question why the disciplinary committee has the power to subpoena any other person when the investigating committee, more appropriately, has the power to subpoena those this specific knowledge of the matter. Our opinion is that section 50(4) should be updated to be consistent with 48(5)(a)(i). We recommend the following amendment.

> *50(4) A Disciplinary hearing panel may, for the purposes of a disciplinary hearing subpoena any person with specific knowledge of the matter being heard to appear before the panel at the time and place specified in the subpoena….."*

Section 50(2) as proposed in the Bill still allows for the charges to be amended post-facto and does not make specific provision for the accused to respond; section 50(3) as proposed in the Bill still makes provision for the hearing to take place in public, which raises privacy concerns; and the drafting of section 50(12) as proposed in the Bill is unclear and difficult to interpret. Therefore, it is recommended that:

- Proposed section 50(2) incorporate an enabling provision in that if the charge is amended, the accused is provided with adequate time to amend / supplement their plea and written representations;
- Proposed section 50(3) be amended such that the default position is that the hearings are held in private and are confidential and that the chairperson may only allow the hearing to take place in public if such right was waived by the accused;
- Proposed section 50(12)(iv) be clarified as the current interpretation is unclear in that the sub-sections appear to be numbered incorrectly.

Section 51 and 51B – Sanctions in admission of guilt and disciplinary process

Under the existing Act version of the APA the fines are determined by the disciplinary committee subject to the Adjustment of Fines Act 101 of 1991 ("Fines Act"). The maximum fine is calculated according to the ratio for five years imprisonment as prescribed in said the Fines Act. The proposed amendments to section 51 and section 51B effectively move the determination of the maximum fine from under the jurisdiction of the Minister of Justice, to the Minister of Finance. We believe that the Act APA should provide guidance and considerations the Minister needs to follow when setting such fines, to ensure that the fines are not arbitrarily set.

Section 51(4) allows for the enforcement committee to order a registered auditor to pay such reasonable costs incurred relating to an investigation. Our only concern at present is that there is presently no mechanism for an auditor to appeal such a cost order or to challenge the reasonability thereof.

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Therefore, we believe that the APA should include provisions providing greater clarity in respect of the disciplinary process itself. Specifically, regarding the registered auditor's rights of appeal to a higher body within the IRBA, or to a High Court with the appropriate jurisdiction. At present there is only the ability to an administrative review which is limited in scope. An appeal which allows the decision, fine / other sections and or cost order to be reconsidered should be provided for.

Section 51 and 51B – Publishing of the Name of the Guilty Registered Auditor

Section 51 uses the word "may" when dealing the publishing of the name of the registered auditor concerned whereas section 51B uses the word "must".

In our opinion both sections should give the IRBA or the Disciplinary Committee the discretion to decide whether or not to publish the registered auditor's name. Publishing of a registered auditor's name is one of the harshest penalties and needs to be considered carefully in the light of the nature of the Act's transgression.