

June 2013

# SOUTH AFRICA

## REPORT ON THE OBSERVANCE OF STANDARDS AND CODES

### ACCOUNTING AND AUDITING



# The World Bank Group



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**SOUTH AFRICA  
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ACCOUNTING AND AUDITING**

**June, 2013**

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## ABBREVIATIONS AND ACRONYMS

AAT(SA)	Association of Accounting Technicians – South Africa
ACCA	Association of Chartered Certified Accountants
AFROSAI	African Organization of English speaking African Supreme Audit Institutions
AG	Auditor General
APA	Auditing Profession Act, 2005
APB	Accounting Practices Board
ASB	Accounting Standards Board
CA	Chartered Accountant
CC	Close Corporation
CFAE	Committee for Auditor Ethics (IRBA)
CIMA	Chartered Institute of Management Accountants
CIPC	Companies and Intellectual Property Commission
CTA	Certificate in the Theory of Accounting
FASSET	Finance, Accounting, Management Consulting and other Financial Services Sector Education and Training Authority
FRIP	Financial Reporting Investigations Panel
FRSC	Financial Reporting Standards Council
FSB	Financial Services Board
GAAP	Generally Accepted Accounting Practice
GDP	Gross domestic product
GRAP	Generally Recognized Accounting Practice
IAASB	International Auditing and Assurance Standards Board
IASB	International Accounting Standards Board
ICSA	Southern African Institute of Chartered Secretaries and Administrators
IES	International Education Standards
IESBA	International Ethics Standards Board for Accountants
IFAC	International Federation of Accountants
IFASS	International Forum of Accounting Standards Setters
IFIAR	International Forum of Independent Audit Regulators
IFRS	International Financial Reporting Standards
IIRC	International Integrated Reporting Committee
INTOSAI	International Organization of Supreme Audit Institutions
IOD	Institute of Directors
IRBA	Independent Regulatory Board for Auditors
IRC	Integrated Reporting Committee
IPSAS	International Public Sector Accounting Standards
ISA	International Standards on Auditing
ISQC	International Standard on Quality Control
JSE	Johannesburg Stock Exchange
King III	King Code of Corporate Governance for South Africa 2009
MFMA	Municipal Finance Management Act
LLP	Limited liability partnership
NQF	National Qualifications Framework
PAAB	Public Accountants and Auditors Board
PAFA	Pan African Federation of Accountants
PAO	Professional accountancy organization
PFMA	Public Financial Management Act
QE	Qualifying Examination
ROSC	Reports on the Observance of Standards and Codes (World Bank)

SAICA	South African Institute of Chartered Accountants
SAIPA	South African Institute of Professional Accountants
SAQA	South African Qualifications Act/Authority
SARB	South African Reserve Bank
SME	Small and medium-size Enterprise
SMO	Statements of membership obligations (IFAC)
SMP	Small and medium-size practice
TEUF	Thuthuka Education Upliftment Fund
WEF	World Economic Forum
WB	World Bank

Exchange rate applied: 1 US\$: Rands 8.3

## PREFACE

The World Bank conducted the second Report on the Observance of Standards and Codes – Accounting and Auditing (ROSC A&A) review in South Africa at the request of the Minister of Finance. The first review was conducted in 2003. The report summarizes the findings and policy recommendations that will contribute in developing a comprehensive reform plan that will strengthen the accountancy and auditing practices in the country with the overall aim of enhancing competitiveness and advancing governance and financial accountability in both private and public sector entities. It presents the status of implementation of 2003 policy recommendations and sets out current systemic issues pertaining to accountancy profession institutional framework that require strengthening. In addition, the report also shares good accounting and auditing practices adopted in South Africa.

The ROSC A&A focuses on assessing the institutional framework underpinning the accounting and auditing practices in the private sector of a country in comparison with international standards and good practices. It evaluates the statutory framework supporting the accountancy professions; education and training of accountants; professional accountancy organizations and ethics; accounting and auditing standards; and monitoring, enforcement, and oversight of the profession. An overview of the ROSC A&A program, including detailed methodology, is available at [www.worldbank.org/ifa/rosc\\_aa.html](http://www.worldbank.org/ifa/rosc_aa.html)

The ROSC A&A review was carried out in South Africa from May to October 2012 through a participatory process involving in-country stakeholders from the Government, regulatory bodies, accounting and auditing firms, insurance companies, banks, and academia. The review was conducted by a World Bank team comprising Patrick Kabuya (Task Team Leader, Senior Financial Management Specialist, AFTME); M. Zubaidur Rahman, (Program Manager, OPSOR, and ROSC Team Adviser); Tandile Ngetu (Financial Management Specialist); Gert van der Linde (Lead Financial Management Specialist); Robert Garnett (Consultant and former member of the IASB and Chairman of IFRS Interpretation Committee); Rhonda Schnare (Consultant and former PCAOB Director); Thomas Zimmermann (Senior Technical Manager, Member Body Development, IFAC); and Lesley Stainbank (Consultant). A special thanks is extended to the peer reviewers: Ian Mackintosh (Deputy Chairman of IASB), Russell Guthrie (Executive Director, IFAC), Fily Sissoko (Lead Financial Management Specialist, AFTMW), Liam J. Coughlan (Senior Financial Management Specialist, CFRR), Chunlin Zhang (Lead Private Sector Development Specialist, FPD), and Szymon Radziszewicz (Senior Technical Managers, Member Body Development, IFAC). The ROSC team acknowledges the guidance provided by Asad Alam (Country Director, South Africa); Patricia Mc Kenzie (Sector Manager AFTME), and Marco Scuriatti (Senior Country Officer).

The ROSC team also acknowledges the contributions made by many stakeholders who were met and participated during the review. The team acknowledges with gratitude the support of the members of Steering Committee under the chairmanship of Mr. Freeman Nomvalo, Accountant General, and staff at the Independent Regulatory Board for Auditors, which served as the review secretariat, with special mention of Mr. Matthew Richardson and Mr. Bernard Agulhas, Chief Executive Officer.

Vice President:	Makhtar Diop
Country Director:	Asad Alam
Sector Manager:	Patricia Mc Kenzie
Task Team Leader:	Patrick Kabuya



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## EXECUTIVE SUMMARY

1. The main purpose of the South Africa Report on the Observance of Standards and Codes, Accounting and Auditing (ROSC A&A) is to determine reforms that will continue to improve the quality of financial reporting in South Africa. The review, requested by the Minister of Finance, was conducted to assess the status of implementation of policy recommendations in the prior 2003 ROSC A&A report, assess the institutional framework underpinning accounting and auditing practices in comparison with international standards and good practices in order to identify any emerging issues that require strengthening, share good practices adopted in the country, and propose policy recommendations addressing areas that require improvements. Implementation of the policy recommendations will further enhance the quality of financial reporting in the country — a key pillar that contributes to enhancing the business environment and advancement of governance and financial accountability in both the private and public sector entities. The review focus on private sector. Financial reporting in public sector are assessed under Public Expenditure and Financial Accountability framework.

### **Strong corporate financial reporting system incorporating global standards**

2. **South Africa has implemented reforms in the past decade that have strengthened corporate financial reporting systems.** All 2003 policy recommendations have been implemented. South Africa enacted the Auditing Profession Act, 26 of 2005, that establishes an Independent Regulatory Board for Auditors. The Board sets auditing and professional ethics standards, and registers and regulates auditors. The Companies Act, 71 of 2008, strengthens financial reporting requirements, including providing legal backing to financial reporting standards. National accounting and auditing standards are fully aligned to the International Financial Reporting Standards (IFRS) and International Standards on Auditing (ISA), respectively. South Africa is one of the earliest adopters of IFRS and ISAs. The country has also adopted principles of corporate governance in the King III Code and requires listed companies to prepare and issue annual integrated reports in place of an annual financial report and a separate sustainability report. These reforms have strengthened the institutional pillars that support the country's accounting and auditing practices: South Africa has been ranked first (out of 144 countries) in the past three years in the annual Global Competitiveness Survey, auditing and reporting standards category, conducted by the World Economic Forum.

3. **The professional accountancy organizations (PAO) continue to contribute in development of more technician and professional accountants to serve public and private sectors, despite a continued shortage of entrants in the field.** There are 12 professional accountancy organizations offering different qualifications and recognized by various regulatory bodies. However, the PAOs are not supervised by any institution in the country in terms of their qualification, capacity, and mechanism of how they monitor their members. Such a situation increases risk of reputational damage to the profession as some members may offer inferior quality services. Further, it limits the recognition and ability to promote the different qualifications offered by the PAOs to prospective accountants, training institutions, and employers. SAICA and SAIPA are globally recognized as premiere bodies. SAICA, the largest PAO in South Africa, plays an instrumental role in thought-leadership initiatives that support protection of public interest and the growth of accountancy profession in South Africa and at a global level. In fact, over 20% of its members work outside the country. The number of PAO members – serving in various accountancy roles - has increased from 39,559 (2003) to 60,843 (2012), up by approximately 54 percent. A study conducted by the South Africa Institute of Accountants (SAICA) during the period from November 2007 to February 2008 shows that there

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was a shortage of 22,000 qualified people to perform financial reporting and auditing functions. A similar conclusion can be construed by comparing the current number of entities in the country i.e. over 1.36m entities (paragraph 1.5), with the number of PAO members. The implication is clear that the country still needs to develop more accountants. On the other hand, there are a significant number of people working as accountants who are not members of any of the recognized professional accountancy organizations—this situation can cause reputational risk to the accountancy profession (paragraph 3.29). There is a need for comprehensive arrangement to supervise and regulate PAOs to ensure that all PAOs serve public interest; a move that would also contribute to enlisting all accountants to be members of PAOs.

4. **The gender and racial representation of professional accountants appears to be improving due to the initiatives being implemented by the Government, professional accountancy organizations, tertiary institutions, and audit regulator (paragraph 3.30).** The Black membership of the professional accountancy organizations has increased during the past 10 years with implementation of the Thuthuka program and various transformation initiatives by universities and professional accountancy organizations; however, more effort in this regard is still required.

5. **The Independent Regulatory Board for Auditors (IRBA) contributes to strengthening auditing practices, especially through supporting auditors to apply stipulated international auditing and ethics standards and conducting audit quality reviews.** The audit quality reviews contribute to strengthening the quality of financial statements. However, opportunities exist for IRBA to improve on the approach, methodology, and rigor of its inspections in order to offer more value, enhance independence of the committees involved in inspections (quality reviews) and disciplinary processes, introduce punitive deterrent sanctions, and put in place follow-up mechanisms of reportable irregularities submitted to different regulators.

6. **The number of auditors in the country has remained almost the same over the past decade.** Currently, in reference to its mandate, IRBA has only accredited SAICA as the Institute whose members, with Chartered Accountants (South Africa)—CA(SA), are eligible to serve as auditors. The number of CA(SA) auditors has increased minimally from 4,197 in 2003 to current 4,252 (May 2012). The low increase is attributed to other competing opportunities: many qualified accountants want to work in commerce and business industries. There is minimal retention of auditors in the profession after they finalize practical training. There is a perception that the unlimited personal liability, the demanding technical knowledge, and the scrutiny by the independent regulator are factors contributing to low retention. The audit partnership law in the country does not allow protection of individual audit partner's assets. And, adding to this mix, the audit profession is no longer viewed as an attractive career.

7. **The CA(SA) qualification remains the first choice by most prospective accountants.** As a result of the strong CA(SA) branding and job prospects for newly qualified chartered accountants, most accounting students enter universities with the intention of qualifying as CA(SA) holders. SAICA has accredited 13 of 23 South African universities to offer the CA(SA) curriculum. Most of the universities have started both CA and non-CA streams. Other professional accountancy organizations have started to enter into partnership with the universities to offer their respective qualification curricula.

8. **The accounting qualifications of most accredited universities focus on accounting and auditing in the private sector.** There is minimal inclusion of public sector subjects in the curriculum—an aspect that is considered critical in order to develop the required financial skills



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to serve the public sector. In fact the number of professional and technician accountants working for public sector remains low (refer to paragraph 6.5 of Chapter 6 in main report).

9. **South Africa has a long history of standard-setting and plays an influential role in standard-setting globally.** The Accounting Practices Board (APB) was responsible for setting national accounting standards prior to enacting the new Companies Act 2008. In 2003, the APB harmonized the recognized national accounting standards—SA Generally Accepted Accounting Practice (GAAP)—with IFRS; and South Africa was the first country to issue local requirements on small and medium-size enterprises (SME) financial reporting based on the International Accounting Standard Board (IASB) exposure draft on IFRS for SMEs in 2008. The IRBA sets auditing and professional ethics standards. The 10-member South African Accounting Standards Board (ASB), established by law, is responsible for issuing public sector accounting standards. The country participates in the international standard-setting process by being members of international standard setting Boards, and committees or work groups, and by issuing comment letters. A Financial Reporting Standards Council (FRSC) has been established in line with the requirements of the Companies Act, though it has not been provided with necessary infrastructure and resources to meet its mandate.

10. **The Financial Reporting Investigation Panel (FRIP), formally the GAAP Monitoring Panel, contributes to improving quality of financial reporting by listed companies.** The joint initiative between the Johannesburg Stock Exchange (JSE) and SAICA was established in 2002 to fill the gap in the previous Companies Act where there were no requirements to review financial statements for compliance with applicable accounting standard. The new Companies Act 2008 also does not include any such requirements. In 2011, JSE invited the University of Johannesburg to be its partner in conducting review of financial statements.

11. **The small and medium-size practices (SMP) face challenges in keeping up to date with the developments in both accounting and auditing standards.** While there are a number of capacity-building opportunities offered to small and medium-size practices, especially by SAICA and IRBA, most still face challenges in understanding and applying the evolving standards. A number of practices also expressed concern of losing their revenue base due to the removal of the requirement to conduct an audit for all companies, as provided in the new Companies Act.

## **Recommendations for a Strong Financial Environment, 2013 and Beyond**

12. To continue strengthening the accounting and auditing practices in South Africa, the Government is presented with the following policy recommendations. These principle-based recommendations are formulated on international good practice and take into account the country context. To implement the recommendations, the Government and country stakeholders should develop a country action plan that incorporates specific objectives to be undertaken, timing (short, medium, or long term), and the institution responsible of implementing each action.

13. **Accountancy profession legislation should be enacted to encompass the regulation of both professional accountancy organizations and an audit regulator.** While regulation exists for the audit regulator, none exists for professional accountancy organizations. The proposed legislation should provide the mandate to create an institution (regulatory body) that would be responsible for (a) defining and categorizing the education and training (frameworks) requirements for different accountancy services (e.g., audit, independent review, accounting officers, bookkeepers) and aligning the PAO qualifications to these respective categories; (b)

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accrediting, registering, monitoring, and sanctioning the professional accountancy organizations; (c) creating awareness of the qualifications of all accredited professional accountancy organizations to employers, tertiary institutions, students and public; and (d) supporting strengthening the professional accountancy organizations, an action that would assist in designing a consolidated plan to develop more accountants to meet the existing demand. Such qualified accountants would contribute in the growth of the expanding economy. An independent board, supported by a well-functioning secretariat, should govern the regulatory body. In this regards, the requirements in the current Auditing Profession Act would be incorporated in the proposed accountancy profession legislation. Such an arrangement would be in line with the practice by the Financial Reporting Council, United Kingdom.

**14. The IRBA inspection methodology and independence of its Inspection and Investigation Committees should be strengthened in line with international good practice.** The inspection methodology should focus on reviewing all applicable auditing standards. The inspection team should reduce its reliance on the firms' internal review to select review files. The team should conduct more robust risk analysis when choosing engagements and particular areas within an engagement review. As well, the inspection methodology should raise the level of experience and expertise of inspection teams and move the Inspection and Investigation Committee functions in-house or reconstitute the committees with no registered auditors serving as members.

**15. The disciplinary process and sanctioning requires independence, rigor, and timely resolution.** The IRBA Disciplinary Committee should not include practicing auditors, and the monetary penalty available under law should be increased from its current maximum limit of R100,000 (US\$12,000) per charge. Names of auditors who are sanctioned through a "settlement order" should be made public – published say in the official IRBA publications. Such an initiative could serve as a deterrent and also increase the visibility of IRBA

**16. IRBA's resources and capacity should be increased, and its funding model should be stabilized.** According to the International Forum of Independent Audit Regulators (IFIAR) core principles, the audit regulator "should have a stable source of funding, which is secure and free from influence by auditors and audit firms and sufficient to execute its powers and responsibilities. In addition, it is a prerequisite that there is sufficient staff of appropriate competence." While IRBA is charged in the Auditing Profession Act with a wide range of responsibilities that are both labor- and cost-intensive, it does not have adequate financial and human resources capacity. IRBA is in need of additional funding to carry out its existing mandate.

**17. The follow-up process of reportable irregularities submitted by the IRBA to the different regulators should be improved to ensure corrective actions are taken.** While conceptually the requirement for auditors (and independent reviewers) to submit reportable irregularities is considered a valuable tool for detecting and deterring wrongdoing, there should be an obligation on the part of the regulator to take appropriate follow-up action on the reported irregularity. In addition, the regulator should be required to report back to IRBA or CIPC (as applicable) on an annual basis as to the dispositions of the reports so that outcomes may be measured. The confidentiality and sensitivity of information should be considered before deciding what to disclose or report back.

**18. South Africa should consider enacting a law that would allow audit firms to organize as limited liability partnerships (LLPs).** The law would contribute in increasing attractiveness of auditing as a career. Since the early 1990s, Germany, India, Singapore, the

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United Kingdom, the United States, and many other countries have passed legislation allowing their audit firms to become LLPs. In an LLP, the personal assets of an audit firm's non-negligent partners are protected in the event of a lawsuit against a negligent partner. In addition, since the LLP legislation does not provide for protection of the assets of the audit firm or the personal assets of negligent partners, South Africa may consider requiring the firms and audit practitioners to carry a sufficient level of professional indemnity insurance.

19. **Professional accountancy organizations and tertiary institutions, where appropriate, should include public sector modules in their education and training curricula.** To address the training needs and capacity shortage in the public sector, it is imperative for professional accountancy organizations and tertiary institutions (in partnership with government) to start including or increasing the use of public sectors modules in their curricula and also creating incentives to motive both students and the providers.

20. **All professional accountancy organizations should be strengthened to have the capacity to increase focus on professional development of their members and improve on their partnerships with universities.** When professional accountancy organizations maintain appropriate capacity, they are able to capture and maintain the public interest; develop capable and competent accountancy professionals; promote and enforce strong professional and ethical standards; and act as a resource to government, regulators, and other stakeholders.

21. **The FRSC should be provided with necessary infrastructure and resources to achieve its mandate.** The Department of Trade and Industry (DTI) should provide the council with resources – financial and adequate and suitably qualified technical and support staff – necessary to meet its mandate.

22. **The proposed legislation to regulate both professional accountancy organizations and an audit regulator (paragraph 13) should require review of financial statements of large public interest entities for compliance with financial reporting requirements.** The requirements should be applicable to companies with a public interest score<sup>1</sup> above a certain limit and to state-owned entities. A unit/division within the regulatory body should be mandated to conduct reviews for compliance with reporting standards and take appropriate actions for noncompliant companies. The unit/division should have adequate capacity of suitably qualified expertise and financial resources. The JSE (currently championing FRIP) should be engaged in establishing the unit/division with a view of transferring the work and mechanics of FRIP to the unit/division.

23. **The SMPs should be encouraged to strengthen their resources and capabilities in order to be competitive in providing professional services.** The SMPs that want to be competitive in the market place need to raise their professional capabilities through expansion. It is worth noting that if an accounting firm is not a viable size, it is difficult for that firm to continuously support enhancement of professional capabilities. Merger of a number of SMPs and/or networking with a regional/international network of accounting firms may be the most

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<sup>1</sup> The public interest score is the sum of the following: (i) a number of points equal to the average number of employees of the company during the financial year; (ii) one point for every R1 million (or portion thereof) in third party liability of the company at the financial year end; (iii) one point for every R1 million (or portion thereof) in turnover (if the company is a holding company, turnover is the consolidated gross revenue of that company and each of its subsidiaries) during the financial year; and (iv) one point for every individual who, at the end of the financial year, is known by the company to directly or indirectly have a beneficial interest in any of the company's issued securities. A company must calculate its public interest score at the end of each financial. The score provides an objective input into the determination of whether a company's annual financial statements require to be audited or independently reviewed,

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effective vehicle for SMP expansion in South Africa. The SMPs should also give more thought to how else they could strengthen resources and capabilities, and how they could focus on alternative service offerings in niche and high value-creating areas. In this regard, they should make reference to the IFAC SMP Committee tools and resources available free of charge on the IFAC website.

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## I. INTRODUCTION

**1.1 The Report on the Observance of Standards and Codes, Accounting and Auditing (ROSC A&A)<sup>2</sup> is aimed at determining reforms that will continue to improve the quality of financial reporting in South Africa.** The review, requested by the Minister of Finance, provides an update on the implementation of policy recommendations in the first ROSC A&A in 2003 and also identifies emerging strengths and weaknesses in the institutional framework that underpin accounting and auditing practices in South Africa. It proposes policy recommendations to address the identified systemic weaknesses and highlights the good practice approaches adopted by South Africa. The specific pillars of the institutional framework that are reviewed include education and training for accountants, the capacity and services of a professional accountancy organizations (PAO) in the country, the regulatory framework governing accounting and auditing practices, the applicable accounting, auditing and ethics standards and the extent of their implementation, and the regulatory institutions and mechanism for monitoring and enforcing compliance with the standards. A strengthened institutional framework will contribute to improving the quality of corporate and public entities financial reporting—key contributors to improving country competitiveness, governance, investor confidence, and ultimately economic growth. The report also shares good accounting and auditing practices adopted in South Africa.

**1.2 The review was conducted from May to October 2012 using World Bank multi-layered review methodology.** The data and information used for review was gathered from a diagnostic questionnaire completed by stakeholders, by reviewing accountancy profession-related documents, and through interviews with many stakeholders from Government, regulatory bodies, accounting and auditing firms, banks, insurance companies, state-owned enterprises, small and medium-size enterprises, and academia. An overview of the ROSC A&A and the detailed presentation of methodologies are available on the World Bank website.<sup>3</sup> The review focuses on assessing the institutional framework underpinning accounting and auditing practices in the private sector of the country in comparison with international standards and good practice.

### Country Context

**1.3 The Government of South Africa endorsed a National Development Plan in September 2012 aimed at eliminating poverty and reducing inequality in the country by 2030.<sup>4</sup>** The plan seeks to eliminate poverty and reduce inequality by drawing on the energies of the country's people, growing an inclusive economy, enhancing the capacity of the state, and promoting leadership and partnership throughout society. Some of the notable critical actions that the plan advocates for implementation include boosting private investment in labor-intensive areas, competitiveness, and exports; and strengthening accountability. Implementation of credible accounting and auditing practices would contribute in achieving these actions.

**1.4 The 2008-2012 Country Partnership Strategy for South Africa, developed jointly with the South Africa National Treasury and World Bank, supports achievement of increased private sector development, capacity building, and sharing knowledge.** Similar to the recently adopted National Development Plan, the Country Partnership Strategy focuses on the eradication of poverty and the reduction of inequality. The strategy consists of two pillars (a) urban and rural development and (b) regional integration, with a cross-cutting theme of capacity

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<sup>2</sup> The ROSC A&A is part of the joint World Bank and IMF initiative on standards and codes.

<sup>3</sup> Access ROSC Accounting and Auditing at [www.worldbank.org/ifa/rosc\\_aa.html](http://www.worldbank.org/ifa/rosc_aa.html)

<sup>4</sup> The income Gini was around 0.70 in 2008 and consumption Gini was 0.63 in 2009 (World Bank South Africa Economic Update July 2012).

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building for public service delivery. A strengthened institutional framework for the accountancy profession contributes toward achievement of these objectives.

**1.5 South Africa continues to improve its business environment in order to attract investments and increase economic growth.** South Africa, with a population of 51.8 million, was ranked 39 out of 185 countries in the 2013 Doing Business Report.<sup>5</sup> The Johannesburg Stock Exchange (JSE) had 399 listed companies with a combined market capitalization of Rand (R)7,284 billion (about US\$876 billion) as of May 17, 2012.<sup>6</sup> The country has a strong banking and financial services sector with 17 registered commercial banks<sup>7</sup> and 196 insurance companies.<sup>8</sup> There are 28,346 non-profit companies; 3,078 public companies; 365,396 private companies; 970,711 close corporations; and 1,415 external companies (these figures include the JSE-listed companies).<sup>9</sup> South Africa's gross domestic product (GDP) in 2011 was US\$408.2, represented a 3.1 percent improvement on 2010, but was down compared to 2007 and 2008. Foreign direct investment inflows were US\$5,717 million. The GDP per capita has been steadily increasing and in 2011 was US\$8,070, up from US\$5,930 in 2007.<sup>10</sup> Investors require comparable financial information from countries competing for foreign investments. Therefore, compliance with globally acceptable accounting and auditing standards and codes adopted by the South African corporate sector is a key contributor to creating an environment that attracts investments.

**1.6 South Africa implemented a number of accountancy profession reforms in the past decade that have contributed to strengthening the quality of financial reporting and governance in the private sector.** The country adopted the international accounting and auditing standards; revised the Companies Act, which enhances reporting requirements; adopted King III governance code; implemented integrated reporting; and introduced initiatives to develop more accountants serving both the private and public sector. In fact, as part of the annual Global Competitiveness Survey conducted by the World Economic Forum (WEF), South Africa ranked first among 144 countries in the survey reports for years 2010-11, 2011-12, and 2012-13 on the strength of auditing and reporting standards. The WEF survey assesses indicators associated with the country's economic and business environment. It is on this premise that the report shares a number of good practices adopted in the country. The sharing principle is in line with World Bank strategy and further reinforced by a statement on September 6, 2012, by World Bank President, Dr. Jim Yong Kim, during his visit to South Africa where he said:

....We are here to learn. South Africa is the place where many innovations have happened, and we want to deepen our relationship with South Africa because we want to learn from the innovations and the achievements that have happened here so that we can share them not only across the continent but with the rest of the world.

## **II. STATUS OF IMPLEMENTATION OF 2003 POLICY RECOMMENDATIONS**

**2.1** The Government of South Africa has substantially implemented all of the policy recommendations in the 2003 ROSC A&A report. The Auditing Profession Act (APA) establishing the Independent Regulatory Board for Auditors (IRBA), which superseded the Public Accountants and Auditors Board, was enacted in 2005. The Government enacted the Companies Act 2008 (effective from May 1, 2011) that stipulates establishment of a Financial Reporting Standards Council (FRSC), prescribes the applicable accounting standards for different types of

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<sup>5</sup> Doing Business reports available for downloading at [www.doingbusiness.org/reports](http://www.doingbusiness.org/reports).

<sup>6</sup> Johannesburg Stock Exchange (JSE) response to 2012 ROSC questionnaire.

<sup>7</sup> South African Reserve Bank (SARB) response to 2012 ROSC questionnaire.

<sup>8</sup> Financial Services Board (FSB) response to 2012 ROSC questionnaire.

<sup>9</sup> Companies Intellectual and Property Commission (CIPC) response to 2012 ROSC questionnaire.

<sup>10</sup> <http://data.worldbank.org/indicator/>.



companies (differential reporting), sets out sanctions for noncompliance with the reporting requirements, and spells out the objectives and functions of the Companies and Intellectual Properties Commission (CIPC). The South African Institute of Chartered Accountants (SAICA) and the JSE established the GAAP Monitoring Panel (2002), now referred to as the Financial Reporting Investigations Panel (FRIP), to monitor compliance with International Financial Reporting Standards (IFRS) by JSE-listed companies. The professional bodies introduced continuous professional development policies to ensure their members remain professionally competent, and incorporate business ethics in their curricula. These commendable achievements (Table 2.1) indicate the Government and stakeholder commitment to improve the quality of financial reporting in South Africa.

**Table 2.1. Status of implementing policy recommendations of 2003 ROSC A&A**

<i>Key 2003 ROSC A&amp;A recommendations</i>	<i>Status as of July 2012</i>
1. Strengthen the enforcement mechanism.	<p>(a) The IRBA, which replaced the Public Accountants and Auditors Board in 2006, conducts audit quality reviews. It instigates investigations and disciplines noncompliant auditors. IRBA has also established a Code of Professional Conduct as required by S21 of the APA. The Code is aligned to Part A and B of the IESBA Code of Ethics for Professional Accountants.</p> <p>(b) SAICA and JSE established the GAAP Monitoring Panel (2002), now FRIP, to monitor compliance with IFRS by JSE-listed companies.</p> <p>It is acknowledged that more needs to be done to extend financial statement reviews to public interest companies (including state-owned entities) based on a predetermined criterion.</p>
<p>2(a). Enact the Financial Reporting Bill and amend the Companies Act to include provisions on legal backing and arrangements for setting accounting standards, including separate IFRS for SME and other companies;</p> <p>(b) Adoption of IFRS and issuance of implementation guidelines on individual standards, including effective punitive measures against violators of the established accounting and reporting standards; and</p> <p>(c) Strengthen the role of the Office of the Registrar of Companies with regards to the annual financial statements submitted by companies.</p>	<p>The Companies Act 71 of 2008 that became effective from May 1, 2011, stipulates establishment of FRSC, prescribes differential reporting, sets out sanctions for noncompliance with the reporting requirements, and spells out the objectives and functions of the CIPC.</p>
3. Include in the mandate of the FSB a specific role with regard to financial reporting by publicly traded companies.	<p>The JSE, which falls under the FSB, requires listed companies to comply with IFRS in terms of its listing requirements in Section 8. The Financial Markets Bill requires an exchange to enforce its listing requirements.</p>

<i>Key 2003 ROSC A&amp;A recommendations</i>	<i>Status as of July 2012</i>
4. Include in the draft accountancy profession legislation provisions specifically focusing on setting up an efficient and effective regulatory framework for ensuring that the practicing auditors discharge their responsibilities properly.	The draft legislation includes in its provisions the role of the oversight body (Part 7, Sections 28-31), the role of the Regulatory Board (Part 1- 4, Section 3-19), inspections requirements (S47), and disciplinary proceedings (S48-51). The requirements are considered to be adequate measures to monitor auditors.
5. The SARB Supervision Department needs to put in place a mechanism, or actively co-ordinate with the proposed FRSC, for systematic monitoring of compliance with accounting and disclosure.	The SARB, through the Risk Management and Compliance Department, has put in place centralized processes to monitor SARB compliance with legislative and regulatory requirements. A SARB official serves as a member of FRSC.
6. Take following steps with regards to professional education and training:  (a) Professional accountancy bodies should introduce requirements for continuing professional education; and  (b) Business ethics should be taught as a separate subject in undergraduate business/accounting programs.	All professional bodies, in reference to IFAC International Education Standards, implement a policy on continuing professional development.  Business ethics forms part of the competency framework and is included in the curricula offered in tertiary institutions and accountancy professional and technician qualifications.

### III. INSTITUTIONAL FRAMEWORK

**3.1** This section evaluates the institutional framework that underpins the accounting profession and the regulation of auditors in South Africa. A strong institutional framework leads to a robust reporting regime and improves the quality of financial reporting.

#### A. Statutory Framework

**3.2** South Africa has implemented comprehensive and up-to-date regulatory reforms in the past decade that support a sound and robust financial reporting regime. The dominant acts in South Africa that provide the statutory frameworks for accountants and auditors are the Companies Act 2008, the Auditing Profession Act 2005, the Banks Act, the Securities Services Act, the Public Finance Management Act, and the Financial Services Board Act.

#### *Companies Act 2008*

**3.3** The Companies Act 2008 provides legal backing for IFRS and IFRS for SMEs, and for strengthening the institutional framework to support enhancement of the quality of financial reporting. Effective May 1, 2011, the Companies Act 71 of 2008, which replaced the Companies Act of 1973 and its accompanying regulations, provides for the establishment of the FRSC, prescribes the applicable accounting standards for different types of companies (differential reporting), and requires either audit or independent reviews by companies depending on their public interest score. The Act requires financial statements together with the annual

return to be filed with the Companies and Intellectual Property Registration Office (CIPC). The Act, administered by the Department of Trade and Industry, incorporates punitive sanctions for noncompliance.

**3.4 The Companies Act regulations codify the application of IFRS by public companies listed on the Stock Exchange.** The regulations also set out the type of financial reporting standards (i.e., IFRS, IFRS for SMEs) applicable to the different categories of companies as set out in Table 3.2. The South African Statements of GAAP were withdrawn effective for financial years commencing on or after December 1, 2012.

**3.5 The Companies Act allows an independent review by an independent reviewer for certain types of companies as an alternative to the conventional audit of annual financial statements.** Under the previous Companies Act, all companies (public and private) were required to have annual external audits. The new Companies Act requires all companies with a public interest score above 350 to be audited by an IRBA-registered auditor. According to the provisions of this Act, companies with a public interest score — computed as set out in Table 3.1 — between 100 and 349 do not have any legal obligation for external audit, provided that their financials were independently compiled and reported. These companies are required to have their financial statements reviewed by independent reviewers. Companies with public interest score between 100 and 349 and with financial statements being internally compiled are under legal obligation to have an external audit.

**Table 3.1 South Africa Public Interest Score Concept**

*Regulation 26 to the Companies Act, 2008*

(2) For the purposes of regulations 27 to 30, 43, 127 and 128, every company must calculate its ‘**public interest score**’ at the end of each financial year, calculated as the sum of the following:—

- (a) A number of points equal to the average number of employees of the company during the financial year;
- (b) One point for every R 1 million (or portion thereof) in third party liability of the company, at the financial year-end;
- (c) One point for every R 1 million (or portion thereof) in turnover during the financial year; and
- (d) One point for every individual who, at the end of the financial year, is known by the company —
  - i. in the case of a profit company, to directly or indirectly have a beneficial interest in any of the company’s issued securities; or
  - ii. in the case of a non-profit company, to be a member of the company, or a member of an association that is a member of the company.

**The four measures could be set out in a table as follows:**

	Points
(a) Average number of employees during the financial year	= 1 point for each employee
(b) For every R1 million of third party liability or part thereof at financial year-end	= 1 point
(c) For every R1 million of turnover or part thereof during the financial year	= 1 point
(d) i. If a profit company, then for every security holder at financial year-end; or ii. If a non-profit company, then for every member of the company or member of an association that is a member of the company at financial year-end	= 1 point

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**3.6 At present, only IRBA-registered auditors and chartered accountants are authorized to act as independent reviewers for companies with a public interest score above 100 points.** For companies with a public interest score of less than 100, the regulations allow that the review may be conducted by a registered auditor, chartered accountant or person who qualifies to act as an “accounting officer,” as defined in terms of the Close Corporations Act.

**3.7 There is concern that the current criterion to become an accounting officer does not provide adequate qualifications to perform independent reviews.** Independent reviews need to be conducted in terms of International Standard on Review Engagement (ISRE) 2400, *Engagements to Review Financial Statements*. Therefore, it would be important for the officers allowed to perform such reviews to be well trained and have experience on applying the standard. On the other hand, independent reviewers who are not registered auditors (and therefore not regulated by IRBA) are not subject to any form of regulatory oversight. The stakeholders interviewed during the ROSC review expressed the need to revisit and agree on the qualification framework of who can conduct independent reviews and the institution (and approach) that should conduct quality reviews on independent reviewers.

**3.8 Owner-managed companies, which have a public interest score of less than 350 and whose annual financial statements are independently compiled, do not require either an audit or review provided that they also did not hold assets in a fiduciary capacity for a broad range of third parties that exceeded R5 million (US\$ 602, 400) at any time during the financial year.** Conversely, if the annual financial statements of such owner-managed companies are prepared internally they are required to be audited if the public interest score is more than 100. Owner-managed companies with a public interest score of less than 100 are exempt from the requirement to have an audit or independent review, again provided that they did not hold assets in a fiduciary capacity exceeding R5 million. The unintended consequence of this is that owner-managed companies that have the internal capability to compile annual financial statements may feel compelled to incur the unnecessary cost of engaging an independent accounting professional to compile their annual financial statements, rather than incurring the significantly higher additional cost of having them audited

**3.9 The Companies Act requires individual audit partners (not the entire firm unless it is a sole proprietorship) to rotate from audit engagements after five consecutive years.** There is a two-year cooling off period if the individual leaves the engagement after having served for two or more consecutive years as the lead partner.

**3.10 The Companies Act created the CIPC that now handles the combined registration of companies and intellectual property rights and enforcement.** CIPC replaced two existing organizations, the Companies and Intellectual Property Registration Office and the Office of Companies and Intellectual Property Enforcement. The Companies Act requires that any financial statements prepared by a company should not be false or misleading in any material respect. The Companies Act also criminalizes the intentional preparation, approval, dissemination, or publication of materially false or misleading statements and requires the CIPC to enforce and report on compliance with financial reporting requirements. The Companies Act regulations impose an obligation on independent reviewers to submit reportable irregularities to CIPC. If the irregularity falls within its scope of authority, CIPC may choose to conduct an investigation; otherwise CIPC is statutorily obligated to refer the report to the appropriate regulator.

**3.11 A company that is required by the Companies Act or regulation (Section 28) to have its annual financial statements audited must file a copy on the date that it files its annual return with CIPC.** The Act currently provides for a right of access to documents filed with the CIPC by any person, unless the information has been determined to be confidential. However, CIPC has recently recommended to the Minister of Trade and Industry that public access to

audited financial statements should be restricted to only public companies. This recommendation appears to ignore the fact that some private companies may have public accountability through a combination of their economic significance and social responsibility.

**3.12 The Companies Act requires public companies and state-owned companies to establish audit committees.** Other companies may also voluntarily establish an audit committee provided it is specified in its memorandum of incorporation. The audit committee should be composed of directors who are not involved in the day-to-day management of the company. Among the responsibilities of the committee would be to nominate the external auditor for approval by the shareholders at the annual general meeting and to determine the audit fee. The audit committee should also pre-approve any non-audit services to be provided by the company auditor. The external auditor of a company is not allowed to perform bookkeeping services and/or prepare financial statements of the same company.

**3.13** Table 3.2 summarizes the requirements in the Companies Act.

*Table 3.2. Summary of Companies Act Requirements – Financial Reporting Standards, Audit and Independent Review*

<i>Category of company</i>	<i>How are financial statements compiled?</i>	<i>Financial reporting standards</i>	<i>Audit or independent review</i>
State-owned companies	Either independently or internally	IFRS (may be modified by requirements of PFMA)	Audit
Public companies listed on an exchange	Either independently or internally	IFRS	Audit
Non-profit companies that: <ul style="list-style-type: none"> <li>• Hold assets in excess of R5 million in a fiduciary capacity</li> <li>• Perform a statutory or regulatory function</li> <li>• Are foreign controlled or state owned</li> </ul>	Either independently or internally	IFRS (may be modified by requirements PFMA) or IFRS for SMEs	Audit
<ul style="list-style-type: none"> <li>• Public companies not listed on an exchange</li> <li>• Other profit companies that hold assets in a fiduciary capacity in excess of R5 million</li> <li>• Companies that meet the requirements of owner-managed, whose public interest score is at least 350 and more than 100</li> </ul>	Either independently or internally	IFRS or IFRS for SMEs	Audit
Other companies whose public interest score is less than 100.	Internally	IFRS or IFRS for SMEs	Audit
Other companies whose public interest score is less than 350 and more than 100	Independently	IFRS or IFRS for SMEs	Independent review

<i>Category of company</i>	<i>How are financial statements compiled?</i>	<i>Financial reporting standards</i>	<i>Audit or independent review</i>
Other companies whose public interest score is less than 100	Internally	As determined by the company	Independent review
Companies that meet the requirements of owner-managed whose public interest score is less than 350 and more than 100	Independently	IFRS or IFRS for SMEs	Not required
Companies that meet the requirements of owner-managed whose public interest score is less than 100	Internally	As determined by the company	Not required

### ***Auditing Profession Act***

**3.14 The Auditing Profession Act 2005 established the Independent Regulatory Board for Auditors (IRBA) to regulate the auditing profession.** The Auditing Profession Act provides that IRBA responsibilities include registration, inspection, and discipline of auditors, as well as the accreditation of professional bodies. This act ended “self-regulation” of the auditing profession in South Africa. IRBA is also given responsibility for setting auditing standards and standards of professional competence, ethics, and conduct for registered auditors. Pursuant to the Auditing Profession Act, a part-time board governs IRBA. The Minister of Finance appoints the IRBA Board, comprising a minimum of 6 and maximum of 10 members. According to the Act, the IRBA Board should not include more than 40 percent practicing auditors. The Act also mandates the establishment of the Committee for Auditor Ethics (CFAE) to assist the IRBA Board by developing rules and guidelines for professional ethics, including a code of professional conduct.

### ***Banks Act***

**3.15 The Banks Act stipulates financial reporting and auditing requirements for banks.** The Banks Act requires that the banks register as a public company before pursuing any bank operations. As a public company, a bank is required under the Companies Act to prepare its financial statements in accordance with IFRS, which are subject to audit and publication. The Registrar of Banks at the Reserve Bank of South Africa issues regulations requiring additional disclosures in financial statements by banks. According to the Banks Act, the Registrar must approve the appointment of a bank’s external auditor.

### ***Johannesburg Stock Exchange and the Securities Services Act***

**3.16 The Securities Services Act, 36 of 2004, regulates securities exchanges in South Africa.** The aim of the Securities Services Act is to increase confidence in the South African financial markets by (a) requiring that securities services be provided in a fair, efficient, and transparent manner and contribute to the maintenance of a stable financial market environment; (b) promoting the protection of regulated persons and clients; (c) reducing systemic risk; and (d) promoting the international competitiveness of securities services in South Africa. The JSE is the



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only securities exchange operating in South Africa, with 399 listed companies as of May 17, 2012.<sup>11</sup>

**3.17 The JSE is a self-regulatory body that both establishes and enforces its own rules and listing requirements for securities trading.** Through its listing requirements and rules, the JSE regulates financial reporting by listed companies. According to the JSE listing requirements, all publicly listed companies are required to present annual financial statements prepared in compliance with IFRS, and audited in compliance with International Standards on Auditing (ISA) by a JSE-approved (accredited) auditor. The requirement for a JSE-approved, accredited auditor was added to the JSE listing requirements in 2008. To qualify as an accredited auditor, the firm must be registered with IRBA, must have demonstrated experience in auditing listed companies, and must have a minimum of three partners. One partner must have demonstrated knowledge of the JSE, and one must be a specialist in IFRS. Audit partners are required to undergo mandatory training in JSE listing requirements. As at September 30, 2012, there are 395 accredited auditors across 34 accredited audit firms (of whom 379 are local accredited auditors across 28 firms). The 34 accredited firms audit the listed companies in the following ratios: 20.4 percent, PricewaterhouseCoopers; 19.3 percent, Deloitte; 18.3 percent, KPMG; 7 percent, Ernst & Young; 9.1 percent, PKF; 6.8 percent, BDO; 6.8 percent, Grant Thornton; and 13.1 percent by the remaining 27 audit firms. Approximately 1.8 percent of South African audit firms are JSE accredited (i.e., 34 out of 1,900).<sup>12</sup>

**3.18 The JSE listing requirements impose other reporting requirements on listed companies, in addition to compliance with IFRS.** Section 30 of the Securities Services Act and paragraph 3.84 of the listings requirements require publicly listed companies to disclose the following information in the annual report: (a) a narrative statement of how it has applied the principles set out in the King III Code,<sup>13</sup> providing explanation that enables its shareholders to evaluate how the principles have been applied; and (b) a statement addressing the extent of the company's compliance with the King III Code and the reasons for noncompliance with any of the principles in the King III Code, specifying whether or not the company has complied throughout the accounting period with all the provisions of the Code, and indicating for what part of the period any noncompliance occurred.

#### ***Public Finance Management Act and Municipal Finance Management Act***

**3.19 The Public Finance Management Act (PFMA) 1999 and Municipal Finance Management Act (MFMA) promote good financial management in the public sector to enable service delivery through effective and efficient use of the limited resources.** The PFMA, applicable for national and provincial government, gives effect to section 216(1) of the Constitution of the Republic of South Africa (Act No. 108 of 1996), which requires national legislation to establish a national treasury and prescribes measures to ensure transparency and expenditure control in each of the three spheres of government. These legislative provisions gain support with introduction of generally recognized accounting practice; uniform expenditure classifications; and uniform treasury norms and standards. The MFMA principles are applicable to local government. The PFMA created the Accounting Standards Board (ASB), which serves the public interest by setting standards of Generally Recognized Accounting Practice (GRAP) for application by public sector entities.

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<sup>11</sup> South Africa is ranked first for 2012/13 in regulation of securities exchange in the World Economic Forum's competitiveness report.

<sup>12</sup> Correspondence from JSE: 4 October 2012

<sup>13</sup> King III is a revised Code of and Report on Governance Principles for South Africa issued by King Committee on Corporate Governance on September 1, 2009, with an effective date of March 1, 2010. The report is a summary of the best international practice in corporate governance.

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## *Financial Services Board Act*

**3.20 The Financial Services Board (FSB), which was created in 1990 by the Financial Services Board Act, regulates non-bank financial services companies and individuals (of which there are 24,213 as of March 31, 2012).<sup>14</sup>** The FSB has broad authority over the JSE, pension funds, insurance companies, financial advisors and intermediaries, and collective investment scheme operators. It performs on-site examinations and has the authority to investigate misconduct and impose sanctions for violations of applicable law within its scope of authority, such as the Pension Funds Act and the Financial Advisory and Intermediary Services Act.

## **B. The Profession**

**3.21** The Accountancy profession is well established in South Africa. There are 12 professional accountancy organizations that are recognized by various regulators in South Africa. The Independent Regulatory Board for Auditors registers and regulates all the auditors in the country. These organizations contribute to the development of the accountancy profession at different levels (Table 3.3).

### *Professional Accountancy Organizations and Qualifications*

**3.22 Each professional accountancy organization offers its own qualification.** Four of these professional accountancy organizations — SAICA, the South African Institute of Professional Accountants (SAIPA), and two UK-based organizations, Association of Chartered Certified Accountants (ACCA) and Chartered Institute of Management Accounts (CIMA) — are IFAC members. All the other professional accountancy organizations are South African based and develop and serve professionals who offer different types of accountancy-related services.

**3.23 There is no overall national supervision of the professional accountancy organizations to ensure that they serve the public interest.** Considering the fact that the professional accountancy organizations pursue diversified objectives, there is a need to have an overall national supervision of all these organizations. At present, various regulators in South Africa recognize the professional accountancy organizations. This illustrates a form of fragmentation of the supervision and regulation that is likely to impact on the quality of the different professional qualifications offered in the country and services offered by the members of various professional accountancy organizations. Further, it limits the recognition and ability to promote the different professional accountancy organizations to prospective accountants, training institutions, and employers. In accordance with the Close Corporations Act (no. 69 of 1984), organizations 1- 9 in Table 3.3 have been recognized by the CIPC as the professional bodies whose membership are authorized to serve as accounting officers for close corporations. The other three organizations (10-12 in Table 3.3) receive recognition by the Financial and Accounting Services Sector Education and Training Authority (FASSET). Pursuant to the South African Qualification Act (58 of 1995) and the National Qualifications Framework Act (67 of 2008) (NQF Act), the South African Qualifications Authority recognizes the qualifications of various professional accountancy organizations at various NQF levels, and establishes a monitoring framework to review the quality of these qualifications.<sup>15</sup> This framework focuses on an organization's professional qualification only; this does not take into account various other

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<sup>14</sup> 2012 FSB annual report.

<sup>15</sup> Due to the recent revision of the NQF Act, the South Africa Qualification Authority is currently implementing a new framework for the recognition of professional accountancy organizations. At this early stage of the process, only SAICA has applied for such recognition.

elements that define a professional accountancy organization. From this perspective, there is a need to establish a comprehensive arrangement to supervise and regulate all professional accountancy organizations in the country.

**Table 3.3. Professional Accountancy Organizations in South Africa**

	<i>Professional accountancy organization</i>	<i>IFAC membership status</i>	<i>Number of members 2003</i>	<i>Number of members 2012</i>	<i>Number of students 2012</i>
1	Association of Chartered Certified Accountants – SA <sup>a</sup>	UK full member <sup>b</sup>	169	399	1,774
2	Chartered Institute of Business Management/ <sup>c</sup>	None	Not available	481	-
3	Chartered Institute of Management Accountants – South Africa/ <sup>d</sup>	UK full member <sup>e</sup>	1,116	1,655	6,185
4	Institute of Accounting and Commerce/ <sup>f</sup>	None	824	780	1
5	South African Institute of Business Accountants	None	86	1,210	50
6	South African Institute of Chartered Accountants/ <sup>g</sup>	Full member	23,500	34,104 <sup>h</sup>	9,850
7	South African Institute of Government Auditors/ <sup>i</sup>	None	221	480	121
8	South African Institute of Professional Accountants	Full member	5,076	7,339 <sup>j</sup>	1,591
9	Southern African Institute of Chartered Secretaries and Administrators/ <sup>k</sup>	None	3,491	2,486	236
10	Association of Accounting Technicians – SA <sup>l</sup>	None	Not established	273	1,029
11	The Institute of Certified Bookkeepers/ <sup>m</sup>	None	2,500	3,358	34,980
12	Institute of Internal Auditors/ <sup>n</sup>	None	2,576	8,278	138
	<b>Total</b>		<b>39,559</b>	<b>60,843</b>	<b>55,955</b>

<sup>a</sup> Membership numbers at December 31, 2011, supplied by ACCA

<sup>b</sup> The parent organization of the ACCA – South Africa, which is UK based, is an IFAC member body. Only parent organizations (as opposed to local subsidiaries) have the possibility to apply for IFAC membership.

<sup>c</sup> Membership numbers at June 30, 2012, supplied by CIBM

<sup>d</sup> Membership numbers at December 31, 2011, supplied by CIMA (2011 data).

<sup>e</sup> UK-based CIMA is an IFAC member.

<sup>f</sup> CIPC only authorizes members of the Institute of Accounting and Commerce who have a diploma in accounting to act as accounting officers.

<sup>g</sup> Membership numbers at June 30, 2012, supplied by SAICA.

<sup>h</sup> In 2012 with a total membership of 34,104 professionals, 10,604 SAICA members worked in public practice; 16,171 members worked in business; 1,360 members worked in the public sector; 663 members worked in education; and 1,308 members were retired. A total of 7,180 accountants were working overseas. (Source: SAICA)

<sup>i</sup> Membership numbers at May 2012: response by SAIGA to ROSC questionnaire.

<sup>j</sup> In 2012, SAIPA membership includes 7,339 full members: 6,090 members worked in public practice, 594 members worked in business, and 10 members worked in academia. (Source: SAIPA)

<sup>k</sup> Membership numbers at June 2012: response by ICSA to ROSC questionnaire.

<sup>l</sup> Membership numbers at January 1, 2012, supplied by AAT-SA,

<sup>m</sup> Membership numbers at April 2012 obtained from <http://www.fasset.org.za>. Membership numbers Skills

**3.24 SAICA, an IFAC member, is regarded as one of the well-developed professional accountancy organizations on the Africa continent.** SAICA is the market leader of professional accountancy organizations in South Africa in terms of membership, with a total of 34,104 members. Its history evolves from 1894 through creation of various bodies before its formal establishment in 1980. SAICA's CA(SA) members are recognized globally. Most prospective accountants in the country aspire to be CA(SA). SAICA has entered into reciprocity agreements with a number of foreign professional bodies,<sup>16</sup> enabling successful CA(SA) candidates to be globally mobile. In fact more than 20% of SAICA members work out of South Africa. With a vision to develop, influence, and lead, SAICA brands CA(SA) professionals as leaders in business in diverse roles. A research report prepared in 2010 and released in April 2011 indicates that 32 percent of chief executives, 75 percent of chief financial officers, and 32 percent of directors of JSE top 194 companies ranked by market capitalization were CA(SA) qualification holders.<sup>17</sup> Only CA(SA) qualification holders are currently accredited to register with the IRBA to provide audit services in South Africa. SAICA is also a member of Global Accounting Alliance.<sup>18</sup>

**3.25 SAICA plays an instrumental role in thought leadership initiatives that support the growth of the accountancy profession in South Africa and globally.** SAICA, governed by a representative Board, has a well-capacitated secretariat with 172 staff members who, in addition to supporting its members, implement thought leadership initiatives – forward thinking ideas and solutions - for national and global benefit. SAICA has over 173 committees (inclusive of regional and district structures) that support the different aspects of SAICA's strategic objectives and contribute to the global accountancy profession agenda. SAICA has met substantially all IFAC statements of membership obligation (SMO) requirements, demonstrating in a proactive and accountable manner its commitment to the adoption and implementation of international standards and good practice. To support its members, SAICA develops implementation guidance on the accounting and auditing standards, offers many continuing professional development events (an estimated 340 per year), and utilizes technology to serve the members e.g. using the social networking application, Facebook. SAICA is commended by being the global leader in developing an on-line guide on IFRS for SME for use by micro entities. SAICA serves as a role model for other professional accountancy organizations in the region and contributes to the regional agenda. It currently hosts the Secretariat of the Pan African Federation of Accountants, established in 2011 to support growth of the accountancy profession in Africa, currently with 39 members from 34 African countries.

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<sup>16</sup> The professional accountancy organizations which have established reciprocity agreements with SAICA are CICA, Institute of Chartered Accountants in England and Wales (ICAEW), Institute of Chartered Accountants of Scotland (ICAS), Chartered Accountants Ireland (CAI), Institute of Chartered Accountants in Australia (ICAA), New Zealand Institute of Chartered Accountants (NZICA), and Hong Kong Institute of Certified Public Accountants (HKICPA). There are 5 members of SAICA who qualified with CICA, 73 members with the ICAEW, 11 with ICAS, 8 with CAI, 11 with ICAA, and 4 with NZICA. (Source: SAICA)

<sup>17</sup> <https://www.saica.co.za/News/NewsArticlesandPressmediareleases/tabid/695/itemid/2916/language/en-ZA/Default.aspx>

<sup>18</sup> The Global Accounting Alliance was formed in November 2005 and is an alliance of 11 leading professional accountancy bodies in significant capital markets. It was created to promote quality services, share information and collaborate on important international issues. It represents 785,000 members in over 165 countries around the globe. The professional accountancy organizations include The American Institute of Certified Public Accountants (AICPA), ICAI, Canadian Institute of Chartered Accountants (CICA), HKICPA, ICAA, ICAEW, ICAS, Institut der Wirtschaftsprüfer in Deutschland e.V. (IDW), Japanese Institute of Certified Public Accountants (JICPA), NZICA, and SAICA.

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**3.26 SAIPA is committed to serve its members and contribute to the South Africa economy.** Since its creation in 1982, SAIPA, like SAICA, has progressively reinforced its activities to become one of the most developed professional accountancy organizations on the continent. SAIPA members (7,339) mainly offer accountancy and tax services and recently allowed independent reviews. SAIPA has a well-capacitated committee and secretariat structure. Like SAICA, it has met substantially all IFAC SMO requirements, demonstrating in a proactive and accountable manner their commitment to the adoption and implementation of international standards and good practice.

**3.27 The local branches of ACCA and CIMA, UK-based IFAC members, contribute to the development of the accountancy profession in South Africa.** ACCA South Africa includes 399 members who are required to meet high-level membership requirements, which are adopted at the global level. CIMA South Africa membership includes 1,655 professionals. Members of ACCA and CIMA are authorized by CIPC to serve as accounting officers, but they are not accredited to offer audit services. Both qualifications are accredited in the National Qualification Framework and have an increasing number of candidates studying for the qualification — 1,774 for ACCA and 6,185 for CIMA. ACCA and CIMA strongly participate in the development of the accountancy profession in South Africa by sharing good practice approaches at the local level. Both the ACCA and CIMA have started to develop partnerships with tertiary institutions in South Africa.

**3.28 Members of another 8 professional accountancy organizations serve in different accountancy roles.** The Chartered Institute of Business Management, Institute of Accounting and Commerce, South African Institute of Business Accountants, South African Institute of Government Auditors, and Southern African Institute of Chartered Secretaries and Administrators are recognized by CIPC as professional accountancy organizations whose members can serve as accounting officers for CC(SA). Accounting officers are required to join the membership of one of the CIPC-recognized organizations. Members of the Association of Accounting Technicians South Africa, Institute of Certified Bookkeepers, and Institute of Internal Auditors of South Africa offer mainly accountancy, bookkeeping, and internal audit services, respectively.

**3.29 Many individuals serve as accountants without necessarily being members of any professional accountancy organization or without being required to meet specific requirements.** Under current legislation, any individual can prepare financial statements, except for Close Corporations. Some practitioners prepare financial statements for a range of entities, without being a member of any professional accountancy organization or without having obtained any NQF qualification. These practitioners are not required to comply with continuing professional development requirements, they do not have to respect any code of ethics, and they are not subject to the investigation and disciplinary mechanisms of any professional accountancy organization. In addition, no professional accountancy organization assists them with the implementation of the required accounting standards applied in the course of their service offerings. This situation is likely to impact negatively on the quality of financial information—a potential springboard for reputational risk for the accountancy profession. On the other hand, it provides an opportunity for professional accountancy organizations to target this group as potential members.<sup>19</sup> A FASSET calculation shown in Table 3.4 indicates that between 5,000 to 6,800 holders of national diploma or first degree in accounting graduates entered the labor market at NQF-level 6 in each year between 2003 and 2009. In addition, there are over 10,000 first-year degree holders who did not enter the Certificate in the Theory of Accounting (CTA) year (equivalent to honors or fourth year at accredited universities) during the period 2006-2011; it is assumed these numbers entered the labor market (Table 3.5). These two examples provide

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<sup>19</sup> The ROSC review team considers the number of such accountants to be high.

evidence that there are many people working as accountants though they are not members of any professional accountancy organization.

**Table 3.4. Number of Entrants to the Labor Market at NQF-level 6**

	2003	2004	2005	2006	2007	2008	2009	Total
National diplomas	3,417	3,657	2,898	3,196	2,920	2,871	3,207	22,166
First degrees	2,131	2,119	2,059	2,556	3,406	3,323	3,621	19,215
<b>Total</b>	<b>5,548</b>	<b>5,776</b>	<b>4,957</b>	<b>5,752</b>	<b>6,326</b>	<b>6,194</b>	<b>6,828</b>	<b>41,381</b>

Source: FASSET, calculated from Department of Higher Education and Training, HEMIS 2000 to 2009.

**Table 3.5 First-year Graduates Who Do Not Enter CTA Year**

	2006	2007	2008	2009	2010	2011	Total
Third year and bridging passes, including UNISA	4,111	4,782	5,070	4,140	4,377	5,140	<b>27,620</b>
Pass and meet entrance requirements for CTA in the following year	1,929	2,937	2,970	3,119	2,681	3,455	<b>17,091</b>
Number of students who do not enter CTA in the following year	2,182	1,845	2,100	1,021	1,696	1,685	<b>10,529</b>

Source: Throughput rates supplied by SAICA.

**3.30 South Africa needs to develop more professional accountants to serve both the public and private sector.** The accountants will contribute in supporting the growth of the expanding economy. A SAICA-commissioned study conducted from November 2007 to February 2008 identifies a shortage of 22,000 qualified people required to perform financial function within the financial and auditing sector (Table 3.7).<sup>20</sup> A comparison of the current number of members in the 12 South Africa PAOs (60,843) - Table 3.3 – with the number of entities i.e. 1,368,946 (paragraph 1.5) also indicates that more qualified accountants are required. In addition, the number is low when compared with other countries which have well developed accountancy professions (Table 3.6). While the professional accountancy organizations are developing accountants separately, there is no consolidated plan on how to address the shortage. Therefore, the profession and the Government should continue to advance the agenda of developing more accountants taking into account the gender and racial representation.

**Table 3.6: Qualified professional accountants in other countries who are members of IFAC members bodies**

Country	GDP 2011 (current US\$) -- m	Population 2010 million	Professional Accountants IFAC PAOs --Thousands (2011)
Australia	1,379,382	22	149
Canada	1,736,050	34	151
United Kingdom	2,445,408	62	287
United States	14,991,300	310	321
India	1,847,976	1,171	221
South Africa	408,236	50	38

<sup>20</sup> *The Financial Management, Accounting and Auditing Skills Shortage in South Africa*, [https://www.saica.co.za/documents/skills\\_long.pdf](https://www.saica.co.za/documents/skills_long.pdf).



**Table 3.7. SAICA-commissioned Study Findings on Shortage of Qualified People in Financial Sector****How many qualified people are needed to alleviate the shortage?**

According to the findings in this research report, at National Qualification Framework (NQF) level 7 and above, 5400 qualified accountants are needed. The total number of vacancies at all levels in both the private and public sectors is 22 030!

Education level	Financial Services Sector			Non-financial Services Sector			TOTAL 2007		
	Filled	Vac	Total	Filled	Vac	Total	Filled	Vac	Total
Grade 11/ NQF Level 3 and below	118	0	118	31 369	379	31 748	31 487	379	31 866
Grade 12 and Diploma or Certificate/ NQF Levels 4 and 5	15 331	1 012	16 342	161 906	6 186	168 092	177 237	7 198	184 435
First Degree/ NQF Level 6	19 110	1 166	20 276	13 222	7 899	21 121	32 332	9 065	41 397
Honours Degree or higher/ NQF Level 7 and above	23 009	1 818	24 826	18 935	3 571	22 506	41 944	5 389	47 333
<b>Total</b>	<b>57 568</b>	<b>3 995</b>	<b>61 563</b>	<b>225 432</b>	<b>18 035</b>	<b>243 467</b>	<b>283 000</b>	<b>22 030</b>	<b>305 030</b>

**3.31 The tertiary institutions, professional accountancy organizations, and IRBA are implementing initiatives to improve diversity of gender and racial representation among members and students to reflect the country's demographics.** The Chartered Accountant Charter entreats the profession “to grow the number of Black people in the [chartered accountant] profession to reflect the country's demographics and sustain the growth of the economy, thereby advancing equal opportunity and equitable income distribution.” SAICA has in particular implemented a Thuthuka initiative (Box 3.1). Universities are actively increasing the number of Black students by participating in the Thuthuka initiative and by allowing entrance into extended or augmented programs for Black students who do not fully meet the admission requirements. Funding for the Thuthuka program has in part come from the Department of Higher Education and Training, the Sector Education and Training Authority, and the National Skills Fund together with private sponsors. The Council for Higher Education reports that from 1994 to 2007 total student enrolments in higher education have grown from 425,000 students to 761,000 students with the proportion of Africans growing from 43 percent in 1998 to 67 percent in 2007. The distribution of enrolments across gender shows that women are entering higher education in larger numbers and that this is consistent with the proportion of women in the country's population. However the demographics of the student participation indicate that African students are still under-represented in total student enrolments.<sup>21</sup> The initiatives are bearing fruit, though more is still required to be done. Black membership of the following professional accountancy organizations has increased from 2003 to 2012 as follows: CIMA, an increase from 2 percent to 7.6 percent; Institute of Accounting and Commerce, an increase from 10.4 percent to 18.7 percent; SAIBA, an increase from 12.8 percent to 51.3 percent; SAICA, an increase from 2.3 percent to 7.0 percent (Table 3.10); and SAIPA, current Black membership comprises 7 percent of total membership. The gender and racial demographics for CTA students has changed dramatically over the past 9 years (Table 3.9). In 2003, the number of female CTA students as a percentage of total enrolment was approximately 28 percent and increased to 50 percent in 2011. Black students comprised 25.8 percent of total CTA enrolment in 2003 compared to 38.8 percent in 2011. Table 3.10 presents a demographic comparison of 2003 and 2012 membership by gender and race.

<sup>21</sup> <http://www.che.ac.za/documents/d000206/>

### Box 3.1 Thuthuka Project

The isiZulu verb *Thuthuka* means “to develop”. The main objectives of this SAICA-driven project, which was launched in 2002, are to increase the number of chartered accountants and to transform the demographics of the profession to match the country’s racial and gender profile and general demand for accounting and auditing services.

The approach of the Thuthuka project is to address the challenges encountered by African and Colored students, from secondary school level through qualification as a chartered accountant, when these students do not have the numeracy and literacy skills to enter the accredited universities leading to a professional qualification nor the financial resources to afford the costs.

The project supports all potential candidates at school, undergraduate, and post-graduate levels. At school level, the main objective has been to ensure that there are sufficient numbers of high-caliber learners able to enter higher education institutions to pursue careers as chartered accountants. The objective is reached, for example, by encouraging school-age students to enter the profession and by helping them to improve their academic skills. At the undergraduate level, the main target is to increase the throughput passes by providing Thuthuka bursary funds, fully supporting students financially, helping them to access additional tutorials, and assisting them in improving their “soft” and life skills. At the graduate level, the project aims to support students from the Thuthuka undergraduate program through their post-graduate studies by specifically supporting the progress of African and Colored students who have failed to pass their examinations but who are identified as having good potential to be successful.

Despite all the challenges, Thuthuka initiatives have had a very positive impact on the demographics of the profession. When the project started in 2002, there were 322 Africans and 222 Colored chartered accountants registered with SAICA. By the end of 2011, these numbers had grown to 2,184 Africans and 873 Colored (Table 3.8). In addition, students graduating from the Thuthuka program have consistently achieved pass rates above the national average of other African and Colored candidates. However, the current demographic profile of the chartered accountant profession still falls short of the demographic ratios of the country, and additional projects similar to Thuthuka would need to be developed to further ensure this gap is addressed.

**Table 3.8 Demographics of SAICA Membership since the Launch of Thuthuka Initiatives**

	<i>Demographics</i> <i>As percentage of total SAICA membership</i>					
	<b>2002</b>		<b>2010</b>		<b>2011</b>	
	<i>African</i>	<i>Colored</i>	<i>African</i>	<i>Colored</i>	<i>African</i>	<i>Colored</i>
<b>CTA students (enrolments)</b>	13%	5%	34%	7%	37%	7%
<b>Trainees</b>	14%	2%	28%	6%	28%	6.5%
<b>Membership</b>	1.5%	1.1%	5.8%	2.5%	6.6%	2.6%
<b>SAICA Membership (number)</b>	<b>322</b>	<b>222</b>	<b>1,845</b>	<b>789</b>	<b>2,184</b>	<b>873</b>

Table 3.9. CTA Enrolments

Year	By gender			By race					
	Male	Female	Total	Black	Colored	Indian	White	Other	Total
2003	3,918	1,516	5,434	1,401	248	1,010	2,775	0	5,434
2004	3,594	3,145	6,739	1,912	371	1,119	3,337	0	6,739
2005	3,268	2,963	6,231	1,862	350	1,108	2,911	0	6,231
2006	3,421	3,347	6,768	1,981	400	1,227	2,956	204	6,768
2007	3,229	3,243	6,472	1,915	414	1,139	2,824	180	6,472
2008	3,251	3,302	6,553	2,013	386	1,272	2,620	262	6,553
2009	3,137	3,116	6,253	2,114	390	1,187	2,305	257	6,253
2010	3,104	3,092	6,196	2,157	391	1,148	2,267	233	6,196
2011	3,177	3,147	6,324	2,453	430	1,067	2,193	181	6,324

Source: SAICA throughput statistics.

Table 3.10. SAICA and SAIPA Membership demographics

		Gender		Race					Total members
		Male	Female	Black	Other	Colored	Indian	White	
SAICA	2003	18,917	4,583	547	55	319	1,399	21,180	23,500
	2012	23,533	10,571	2,375	120	925	3,233	27,451	34,104
SAIPA	2003	Unavailable		Unavailable					4,976
	2012	4,695	2,644	515	85	223	592	5,924	7,339

Source: SAICA and SAIPA.

### Auditing Profession

#### 3.32 The Independent Regulatory Board for Auditors regulates the auditing profession.

IRBA, a statutory body created on April 1, 2006, under the supervision of the Ministry of Finance, succeeded the Public Accountants and Auditors Board (PAAB), which was a self-regulatory body for the profession. IRBA's objectives are aimed at protecting the financial interest of the South African public and international investors in South Africa through the effective regulation of audits conducted by registered auditors, in accordance with internationally recognized standards and processes. IRBA's responsibilities include the registration, inspection, and discipline of auditors; accreditation of professional bodies; and setting auditing standards and standards of professional competence, ethics, and conduct for registered auditors. IRBA is an active member of the International Forum of Independent Audit Regulators (IFIAR). The IRBA Board has 10 members, including 4 practicing auditors; a committee structure supporting different roles of IRBA; and a secretariat headed by a chief executive officer with approximately 65 full-time staff. In 2010, IRBA adopted a new Code of Professional Conduct and new disciplinary rules. The new Code, which is based on Part A and B of the IESBA Code of Ethics for Professional Accountants, adopts a "threats and safeguards" approach to ensuring the independence of auditors.

**3.33 The Auditing Profession Act provides that IRBA is funded through three sources: (a) mandatory fees levied on registered auditors to cover the costs of examination, registration, and inspection; (b) appropriations made by the Parliament; and (c) revenue accruing from its own operations such as sanctions.** The Minister of Finance must approve IRBA's budget. The National Treasury has recently asked IRBA to consider ways in which its funding model could be revised such that it becomes less dependent on government funding.

Currently, the National Treasury contributes approximately R30 million (43 percent of total budget) to IRBA's budget. The total budget for financial year ending March 31, 2013, equals R82 million, or approximately US\$10 million. To ensure continued independence and compliance with the IFIAR principles, the ROSC review team considers that continued Government funding remains critical.

**3.34 IRBA has registered 4,252 individual auditors and 1,900 audit firms that employ almost 9,000 professional staff.** IRBA, in reference to its mandate, has only accredited SAICA as the Institute whose members, with CA(SA) qualification, are eligible to serve as auditors. The number of registered auditors has increased minimally since 2003 (when there were 4,197 registered auditors). Seventy percent of the registered auditors perform the attest (audit) function. Audit practitioners indicated that, in their view, the low increase of auditors is attributed to their minimal retention in the profession especially due to unlimited personal liability, onerous regulations and sanctions, and demanding technical requirements. In addition, there is a perception that the audit profession is no longer viewed as an attractive career. Concern was also expressed for the age profile of the members: 65 percent of the members are over age 40. Also, the White community dominates the audit profession at 82 percent. More needs to be done at the professional qualification level not only to improve the racial representation but also to increase female membership, which is currently at 20 percent (Table 3.11). IRBA mainly relies on the transformation efforts of SAICA to rebuild the numbers of registered auditors. In addition, IRBA is managing a support program for Black candidates on an annual basis. There is no mutual recognition of auditors between South Africa and other countries.

**Table 3.11. IRBA Membership Statistics by Gender, Race, and Age**

Age range	Attest		Gender		Race					Total members	
	YES	NO	Male	Female	Black	Chinese	Colored	Indian	White		
[25-29]	91	50	86	55	18	2	0	24	97	141	3%
[30-39]	978	371	873	476	154	2	32	160	1,001	1,349	32%
[40-49]	828	349	920	257	69	2	23	116	967	1,177	28%
[50-59]	591	286	821	56	27	2	12	104	732	877	21%
[60-69]	378	155	520	13	4	1	1	23	504	533	13%
[70-79]	101	54	155	0	0	0	0	1	154	155	4%
[80-89]	6	13	19	0	0	0	0	0	19	19	0%
[> 90]	1	0	1	0	0	0	0	0	1	1	0%
<b>Total</b>	<b>2,974</b>	<b>1,278</b>	<b>3,395</b>	<b>857</b>	<b>272</b>	<b>9</b>	<b>68</b>	<b>428</b>	<b>3,475</b>	<b>4,252</b>	100%
	70%	30%	80%	20%	6%	0%	2%	10%	82%		

Source: IRBA membership statistics May 10, 2012

**3.35 The Auditor General of South Africa is mandated to perform the audit of all public sector entities.** The Constitution of the Republic of South Africa (Act 108 of 1996) establishes the Auditor General (AG) as the external auditor of all National and Provincial state departments and Municipalities, and any other institutions required by legislation to be audited by the AG. It further requires the AG to submit audit reports to Parliament and the Provincial Legislature. The Public Audit Act (PAA) gives effect to the constitutional provisions by further defining the mandate, audits, status and functions of the Auditor General of South Africa (AGSA). The office, with a staff compliment of 2,800, mainly conducts financial audits, performance auditing, auditing of performance information, and audits of compliance with legislation. These audits are performed in accordance with standards defined by AGSA. The Auditor General is mandated to opt out from conducting audit of state-owned entities, which can be done by private audit firms in

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accordance with PAA and AGSA audit standards. The AGSA annually contracts out some audit assignments to private firms. The AGSA contributes to growth of the accountancy profession: it serves as an accredited practical training office for CA(SA) students and registered government auditors as accredited by SAIGA. Currently the AGSA have 900 CA(SA) trainees and 50 SAIGA trainees. It provides bursaries for these trainees as well as to full time undergraduates students from previously disadvantaged communities. The Auditor General contributes to work of the International Organization of Supreme Audit Institutions (INTOSAI), capacity development in Africa through the African Organization of English-speaking Supreme Audit Institutions (AFROSAI) and development of auditing standards through participation in IRBA.

## C. Education and Training

**3.36** Each professional accountancy organization in South Africa offers its own education and training curriculum process. The education requirements, training providers, assessments, and practical training requirements are different and encompass the principles in the International Education Standards (IES) issued by the International Accountancy Education Board, an independent standard-setting board supported by IFAC.

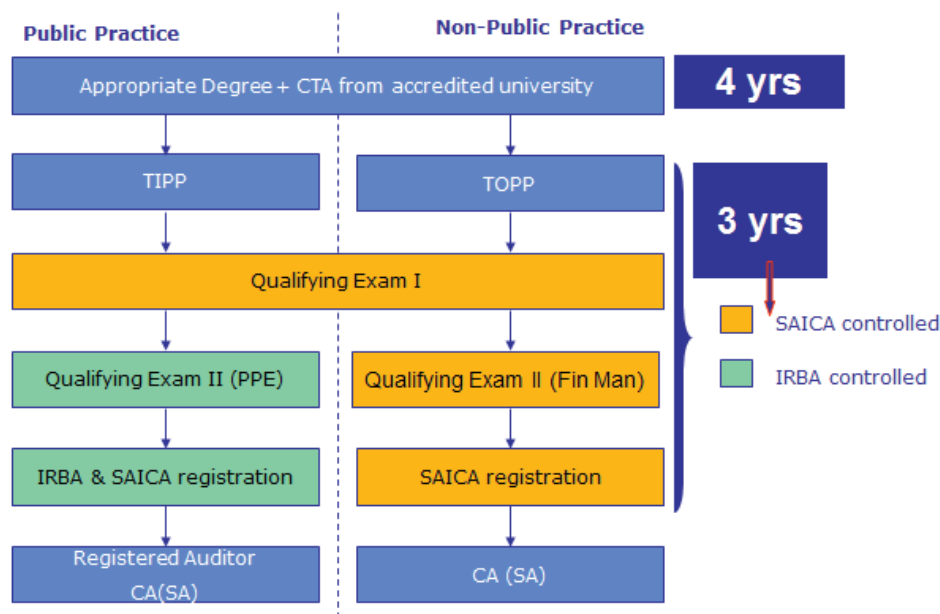
**3.37 SAICA offers a rigorous education program.** The SAICA education program is based on IES and global best practice, including a competency framework. However, due to the poorly prepared students entering the profession from secondary school and the rigor and demands of the program, there is a low throughput rate in universities and during the training contract.<sup>22</sup> As a result of SAICA's strong branding and excellent job prospects for newly qualified CA(SA) holders in the market, most accounting students enter universities with the intention of becoming CA(SA) qualified; and as a result, the main focus of accredited universities is on the CA(SA) program.

**3.38 The SAICA education model (Figure 3.1), leading to the qualifying exams Part 1, is only offered at accredited universities as a four-year program.** Currently, 13 universities have been accredited by SAICA to offer the full four-year program. SAICA is heavily involved in partnering and supporting these universities and in increasing the number of accredited universities in order to offer more opportunities to study toward the CA(SA) qualification. SAICA is supporting non-accredited universities to become accredited especially by using twinning arrangements between accredited and non-accredited universities. The support has resulted in two universities (Monash and Limpopo) now offering the program up to the third year, and another two universities (Walter Sisulu and Zululand) are working toward accreditation at third-year level. The Limpopo twinning arrangement experience set out in Box 3.2 shares key factors that contributed to its success. In addition, SAICA provides financial support to academic staff of accredited universities through salary subvention. The subvention funds are obtained from a portion of the trainee levy, which is distributed to universities based on a formula that takes into consideration the: (a) quality (QE results), (b) quantity (undergraduate, CTA and QE numbers), and (c) transformation. The strong partnership between SAICA and accredited universities has hence increased SAICA's influence on universities' accountancy profession curricula; on the flip side, some consider SAICA's influential role to be a hindrance to access by other professional accountancy organizations.

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<sup>22</sup> Fasset Sector Skills Plan Update for the Period 1 April 2012 to 31 March 2017. Available [www.fasset.org.za](http://www.fasset.org.za).

Figure 3.1. SAICA Education Model



**3.39 To enhance the development of professional skills and competencies, there have been a number of revisions to the professional education and training program for SAICA qualification.** This has been in response to further strengthening its compliance with the IES and also to develop the necessary professional skills and competencies. On January 1, 2010, SAICA implemented the new CA(SA) Training Program, which encompasses the basic set of skills required by a chartered accountant after completing their training program.

**3.40 IRBA is also strengthening its requirements to register as an auditor.** IRBA is currently proposing that after qualification as a professional accountant, a prospective registered auditor will require a further two-year, post-qualification for professional accountant, plus 1,500 billable hours in audit and assurance services. Documented evidence and completion of a practice management workshop will provide the basis for initial registration as a registered auditor.

**Box 3.2 University of Limpopo: Journey to be an Accredited University**

SAICA recognizes that it is important to increase the number of universities that offer the accredited accounting program. To that end, SAICA facilitated the “twinning” of the University of Limpopo with the University of the Johannesburg. This arrangement began in 2004 and culminated with the University of Limpopo’s undergraduate degree being fully accredited in 2012.

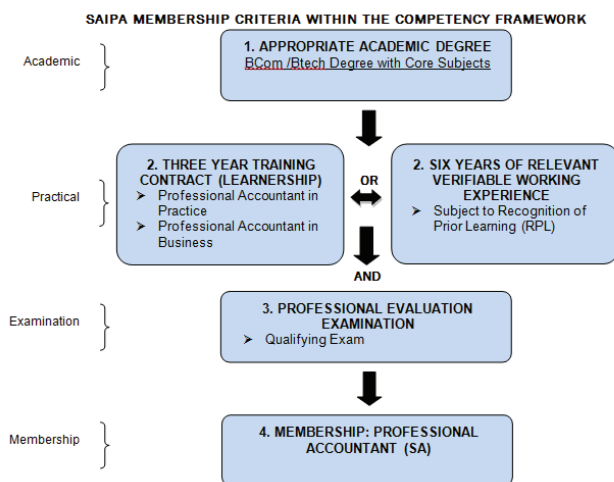
Teaching and learning was enhanced through implementing an effective tutorial system and the use of a variety of formative assessments. This project will not only increase the number of Black chartered accountants in South Africa but will also provide the Limpopo Province and its rural students with access to quality education and an opportunity to qualify as chartered accountants.

A lesson learned from the Limpopo twinning experience and embedded into the new twinning arrangements is that capacity building at the accreditation-seeking institution is crucial. Academic staff members should be fully skilled and resourced to function independently when the twinning arrangement ceases. The turnaround strategy includes ensuring the buy-in from top management, communication with stakeholders, and staff and student ownership and commitment to the program.



**3.41 SAIPA is working toward developing an accreditation model similar to that of SAICA and has begun accrediting universities.** The SAIPA education program is achieved through a three-year university program (Figure 3.2). The SAIPA arrangements with universities are not as stringent as those of SAICA.

**Figure 3.2. SAIPA Qualification Model**



*Source: SAIPA*

**3.42 The professional education and training requirements for audit practitioners continues to be of a high standard.** As mentioned earlier, only CA(SA) holders are accredited to offer audit services. The IRBA, in reference to Auditing Profession Act, took the decision in 2006 to accredit education, training, and assessment programs for professional accountancy organizations for the purpose of achieving requirements to register as an auditor. At the time, IRBA decided to continue to set and administer the Professional Practice Examination (PPE) itself. IRBA published its accreditation model in 2007. In terms of this model, IRBA (like its predecessor PAAB) has only accredited the education, training, and assessment program offered by SAICA. Therefore, as noted above, to become a registered auditor, a CA(SA) holder must register with IRBA.

**3.43 Universities also offer programs that lead into other accountancy qualifications.** In 2003 South Africa began a radical restructuring of its higher education sector. The number of universities was cut from 36 to 23 through incorporations and mergers in order to break down Apartheid's racial divides and transform the sector. These 23 universities are divided into three categories: traditional universities, comprehensive universities, and universities of technology. The interactions with professional accounting organizations are mainly with the traditional and comprehensive universities, with little or no interactions with the universities of technology. Some universities have started partnering with ACCA and CIMA with aim of allowing students certain subject credits to complete the ACCA or the CIMA qualification.

**3.44 Most of the universities have introduced CA and non-CA education streams.** The approach provides access to more students to study for accountancy-related qualification. In addition, it allows other professional accountancy organizations to partner with universities. Some universities have established a College of Accountants or a School of Accountancy. The

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Skills Shortage Report, commissioned by SAICA,<sup>23</sup> notes that the poor standard of secondary schooling impacts directly on the supply of accountants to the market since secondary schooling is the first link in the supply chain of accountants. The report notes that students entering tertiary-level institutions lack adequate mathematical skills and the analytical and comprehensive problem-solving competencies needed to integrate knowledge and make linkages between different accounting and commerce subject areas. The SAICA report further notes that more effort is needed at secondary-level schools; it is not the primary role of universities to bridge gaps left by primary and secondary education. Statistics provided by SAICA on first-year enrolments (CA education stream) in the SAICA-accredited universities shows an insignificant growth in enrollments in the years 2006 to 2011.

**3.45 The curriculum of most accredited universities is focused on accounting and auditing in the private sector.** Little attention is paid to the public sector: an aspect that is considered limiting to the development of skills required to serve the public sector.

## **D. Setting Accounting Standards**

**3.46** South Africa became one of the earliest countries to adopt IFRS as issued by IASB. The Accounting Practices Board (APB), an independently constituted body of academics, preparers, users, and auditors, was formed in 1973 to consider and, shortly after, issue, what would be the generally accepted accounting practice (GAAP) in South Africa. SAICA served as secretariat of APB. In 1993, APB launched the Harmonization and Improvements Project, which revised SA GAAP in line with IAS and issued new standards in all areas where IAS existed.

**3.47 In 2003, the APB harmonized SA GAAP with IFRS and has since then, after due process, issued IFRS as SA GAAP without amendment.** This process continued until May 2011 when the APB ceased approving individual IFRS as SA GAAP. In order to reduce the burden of issuing each new or revised IFRS standard as SA GAAP, the APB withdrew SA GAAP. Accordingly, SA GAAP will no longer apply to financial year reporting commencing December 1, 2012. The APB has responded to a need for an authoritative interpretation of SA GAAP for specific aspects that only occur in the South African context. Such aspects, transactions, or other issues are not specifically or clearly addressed in IFRS. These matters include accounting for Black Economic Empowerment transactions; the interaction of IAS 19, *Employee Benefits*, and the South African pension fund environment; and determining when changes to the South African Income Tax Act should be considered enacted. These authoritative interpretations are referred to as the AC500 series and remain applicable. In 2008, APB also issued an SA GAAP on IFRS for SME based on IASB-issued exposure draft: this made South Africa the first country in the world to adopt IFRS for SME.

**3.48 The Companies Act established the FRSC to advise the Minister of Trade and Industry on matters relating to financial reporting standards.** The FRSC is established to receive and consider any relevant information from the CIPC and other sources relating to the reliability of, and compliance with, financial reporting standards. It advises and consults with the minister on matters relating to financial reporting standards, including the making of regulations that establish financial reporting standards and requirements for the form and content of the summaries of financial statements, and adapting international reporting standards for local circumstances, including development of authoritative interpretations for specific issues that only occur in South Africa. The Minister may request the FRSC to be a member of a relevant

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<sup>23</sup> <https://www.saica.co.za/News/SkillsShortageReport/tabid/1155/language/en-US/Default.aspx>

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international accounting standards-setting organization – to represent South Africa and contribute to the work of such a standard-setting organization.

**3.49 The Minister of Trade and Industry issued a regulation prescribing the application of IFRS or IFRS for SME with respect to all companies that require financial reporting standards.** Therefore, the FRSC has no role in setting applicable accounting standards in the country. However, the FRSC has an important role of participating and influencing the IASB in its accounting standard-setting process and participating in global national standard-setting initiatives. In fulfilling these roles, the FRSC draws on the expertise and technical resources of South Africa accountancy bodies, regulators, and business and investment professionals.

**3.50 The Minister has appointed members of the FRSC although he has yet to provide the FRSC with necessary infrastructure to fulfill its mandate.** The appointed members of the FRSC include auditors; preparers of financial statements for both public and private companies; security holders or creditors who rely on financial statements; company law experts; and representatives from the FSB, South Africa Reserve Bank (SARB), and JSE Securities Exchange. Despite being supported by the Department of Trade and Industry, the FRSC has not yet been allocated a secretariat or budget support necessary to fulfill its mandate.

**3.51 South Africa influences standards-setting processes at regional and international level through proactive participation and contributions to international boards, committees, and forums.**<sup>24</sup> The participation assists the standard-setters who benefit from South Africa's and other regional-specific experiences that enrich development of global standards. The fact that South Africa adopted international standards in the early 2000s has enabled it to accumulate a rich body of implementation experience and know-how.

**3.52 South Africa has a long history of setting standards and has well-developed and well-respected structures and procedures for consulting with those interested in the development of financial reporting standards.** In order to continue to provide significant input to the development of standards at national and international level, it is important to maintain and enhance existing structures. All professional accounting organizations should be involved in contributing to standards-setting processes.

**3.53 South Africa has developed national public sector accounting standards.** The ASB has set a suite of GRAP standards that require application by all public sector entities except government business enterprises, which are profit oriented and hence required to apply IFRS. The accrual-based GRAP standards are grounded on IPSAS and IFRS and developed through a sound consultative due process. All public sector entities excluding national and provincial departments apply the GRAP standards. National and provincial departments are not yet applying the standards as the Government is putting in place the required pre-requisites; instead they apply a reporting framework developed by National Treasury.

## **E. Setting Auditing Standards**

**3.54 IRBA, as mandated by the Auditing Profession Act, is responsible for setting auditing standards as well as standards of professional competency, ethics, and conduct for registered auditors.** Upon its establishment, IRBA confirmed the adoption of the International Standards on Auditing and other pronouncements as issued by the IAASB, IFAC's independent

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<sup>24</sup> South African accountants pro-actively contribute to the IASB (and its many committees and working groups), IFAC (and its boards), the International Forum of National Standard Setters, INTOSAI, AFROSAI, Pan African Federation of Accountants, East and Southern African Association of Accountants General, the Global Accounting Alliance, and the International Integrated Reporting Committee.

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standard-setting body, to be applied by registered auditors in South Africa. The continuing adoption and prescription of IAASB standards, as set by IRBA's predecessor, PAAB, in 2005, for use by all registered auditors in South Africa is made legally effective by IRBA publishing periodic (usually annual) notices in the Government Gazette. Thus, ISA issued by the IAASB in 2009 have been officially adopted for use in South Africa. IRBA also has mandate to develop and issue its own authoritative and non-authoritative pronouncements with regard to auditing and other professional standards. The authoritative pronouncements issued by IRBA are to be consistent with the principles of the international standards but may provide implementation requirements or application material on a particular subject.

**3.55 The Committee for Auditing Standards assists and advises IRBA in its standard-setting activities.** The Auditing Profession Act provides that the Committee for Auditing Standards should have at least 12 members and sets forth required characteristics for certain members. The Committee members are not full-time employees of IRBA. Currently, the Committee has 15 members, including six practicing auditors. The primary functions of the Committee include reviewing ISAs and other pronouncements as issued by IAASB and advising the IRBA Board on their adoption; preparing comments on IAASB exposure drafts; and developing and drafting IRBA pronouncements (i.e., guides, practice notes, and communiqués). The Committee for Auditing Standards follows a robust procedural and consultative process. To date, the Committee has assisted the IRBA Board in finalizing 5 auditing practice statements, 5 guides, and 1 circular.

**3.56 The Auditor General is mandated to determine standards for conducting the audit of public sector entities.** The AGSA applies the International Standards on Auditing and Assurance pronouncements issued by the IAASB in its annual audits. In addition, consideration is made of the relevant principles contained in the International Standards of Supreme Audit Institutions (ISSAIs) and the INTOSAI Guidance for good governance.. The Auditor General is involved in developing International Standards for Supreme Audit Institutions.

## **F. Monitoring, Compliance, and Enforcement**

**3.57** Monitoring occurs in both accounting and auditing sectors. Inspections, with regards to auditing, cover compliance with auditing standards, the design and implementation of the quality control system, audit engagements, and improper conduct. Monitoring of compliance with accounting standards is only done by the JSE for listed companies.

### **1. Auditing inspections**

**3.58 The Auditing Profession Act gives IRBA the authority to inspect any registered auditor and mandates that IRBA inspect the auditors of public interest companies (which include listed companies) at least once every three years.** The Auditing Profession Act allows IRBA to recover the costs of an inspection from the inspected firm. In addition, the Auditing Profession Act requires that registered auditors cooperate with IRBA during inspections by producing any information requested, even if the requested documents include confidential information. The Auditing Profession Act requires that IRBA personnel maintain confidentiality with certain exceptions on any information received during an inspection. Among these exceptions are sharing such information with domestic and foreign regulators under certain circumstances. A registered auditor must give his/her consent to IRBA before it may share information with a foreign regulator.

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**3.59 IRBA has adopted guidelines that set forth the scope, objectives, and process for inspections in reference to international standards.** The IRBA-adopted guidelines (entitled the Manual of Information, which is updated each year) provide that a firm inspection covers both the quality control system of the firm and a sample of audit engagements. The objectives are to inspect the design and implementation of the quality control system and a sample of audit engagements to monitor compliance with the relevant professional standards (e.g., ISQC 1, *Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements*; and ISA).

**3.60 As currently structured, IRBA’s inspection process is influenced by the auditing profession through the statute-mandated Inspections Committee.** The Auditing Profession Act requires the establishment of an Inspections Committee but does not set forth its functions or objectives. Because the statute does not speak to the Committee’s functions, the IRBA Board has wide discretion in determining the Committee’s responsibilities. IRBA’s 2012 guidelines state that the responsibilities of the Committee include determining the nature of attest engagements subject to inspection; assessing the appropriateness of the standard documentation used in the inspection process; determining the outcome of inspections on an anonymous basis; and assessing the quality and consistency of inspection reports. The Auditing Profession Act also leaves the number of Committee members and their qualifications to be determined by IRBA. The Inspections Committee comprises 8 individuals and most recently includes 4 practicing auditors. The guidelines specify that 1 Committee member be an IRBA Board member. Until 2012, the Committee had been composed entirely of practicing auditors. The current Committee chairman is a practicing auditor. The ROSC review team is of the view that the involvement of practicing auditors compromises the desired independence of the Committee, which is likely to negatively impact on the inspection review findings.

**3.61 IRBA’s approach to inspections is sound as a matter of principle but not sufficiently rigorous as a matter of practice.** Consistent with a risk-based approach, the IRBA Inspections Department focuses on registered auditors that audit listed companies and other public interest entities. These firms are subject to inspection at least once every three years. In addition, IRBA conducts engagement reviews at the 4 largest audit firms every year. IRBA has adopted an integrated approach such that the results of the engagement reviews are considered in the context of the review of the firm’s quality control system. The Inspections Department annually selects the specific engagements to be reviewed, but they strive to include at least 40 percent listed companies. The remaining 60 percent are either engagements of other public interest entities or audits of state-owned enterprises. The Inspections Department may alter its engagement selections based on publicly available information or information provided by another regulator such as the FSB or the JSE. The Inspections Department does not otherwise perform a comprehensive risk analysis before selecting the engagements or when determining the specific areas to review within the engagements selected. Of the 658 total engagements reviewed during 2011, 10 percent were found to have deficiencies and almost all of those related to inadequate audit documentation. Of the 218 engagements of public interest entities reviewed, 214 were rated satisfactory. Over the past 3 years, only 3 cases arising out of inspections have been referred from the Inspections Department to the Investigating Committee (*para 3.69*).

**3.62 Although IRBA has the authority and stated objective to review for compliance with all professional standards, in practice its primary focus during engagement reviews is audit documentation.** IRBA’s most recent annual report and most recent public inspection report of public interest entity auditors both describe almost all the deficiencies found during the engagement reviews as relating to audit documentation. IRBA management also confirmed that compliance with audit documentation requirements is the “core” or “driving” principle of inspections. Only infrequently will the inspections team assess for compliance with other auditing

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standards or accounting standards. During the ROSC review, some members of the auditing profession described IRBA inspections as a “box-ticking” exercise that adds little value to either investors, the public, or the auditor because the reviews do not focus on the actual risks in the audits and IRBA inspectors do not have sufficient experience or expertise.

**3.63 The IRBA inspection program is considered to be understaffed and without adequate experienced capacity given its mandate, scope of authority, and number of required reviews.** IRBA began its inspection program soon after its establishment in 2006 with an average of 15 inspectors. It currently has a full-time technical staff of 2 team leaders and 8 other professionals who conduct the inspections. In 2011, the budget for IRBA inspections equaled R15.7 million (approximately US\$1.9 million). The experience of IRBA’s inspectors ranges from 5 to 25 years, with most having closer to 5 years of experience. The sheer volume of expected auditor review, as elaborated as follows, is a resource constraint that adversely affects IRBA’s performance as a regulator:

- IRBA inspects auditors of public interest entities at least once every three years and all other auditors once every six years.
- Currently, there are 4,252 auditors (about 1,900 audit firms, 380 sole practitioners, and 2,974 attest practitioners) registered with IRBA, including the members of the big four international firm networks. These audit practices in the country altogether employ about 9,000 professional staff.
- There are 399 listed companies with a combined market capitalization of R7,284 billion (about US\$876 billion) as of May 17, 2012. These include some extremely large companies with highly complex and sophisticated operations. The lead audit partners for listed companies and other major public interest entities usually have 25 to 30 years’ experience.
- In addition to the listed companies, there are tens of thousands of other public interest companies in South Africa within IRBA’s authority. An inspection of a big four affiliate will typically take a team of 6 IRBA inspectors 8 to 9 weeks to complete. Of that team, 4 inspectors will review the firm’s quality control system and 2 inspectors will conduct the engagement reviews.

For the fiscal year ending March 31, 2011, the 10-member staff of the Inspections Department inspected 658 engagements and reviewed the quality control systems of 22 firms. Based on the demand, the ROSC team considers the inspection team not adequate and not appropriately experienced to aptly review audit files of the more experience partners.

**3.64 IRBA inspections are funded though annual fees imposed on the audit firms.** The fees are based on a percentage of the firm’s audit and other assurance fees related to “high” or “special” risk audits. The firms are asked to disclose the invoiced fees for each audit client and in an annual declaration filed with IRBA to categorize their clients as high, special, or low risk. IRBA provides the category descriptions. For example, high-risk clients include listed companies, registered financial institutions, medical schemes, and significant subsidiaries of both domestic and foreign companies. Special-risk clients must have revenue equal to or more than R50 million (US\$ 6m); this category includes non-profit organizations, public companies, and trade unions. Low-risk clients include all other audit clients that do not fall under high risk or special risk. Until 2012, IRBA charged firms for the actual time spent carrying out the inspection at a standard rate per hour for each inspector. This created an environment where there was pressure to complete the inspection within the shortest time possible. It also raised a concern that IRBA’s independence from the audit profession was being compromised.



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**3.65 A framework and process to conduct quality reviews of independent reviewers has not been developed.** As noted, the Companies Act allows some entities to be subject to independent review. However, the mechanism and framework, for which the entity will be responsible, has not been formulated for reviewing the quality of independent reviews (similar to audit inspections), the review process, and sanctions for noncompliance.

**3.66 IRBA has entered into partnership with the Auditor General to conduct quality reviews on audits done by the Auditor General of South Africa.** Although having no legal oversight role over the Auditor General, IRBA entered into an agreement with the Auditor General in 2000 to review and provide credibility to internal quality control monitoring process by the AGSA. The objectivity of the process assures the Auditor General that his/her office consistently delivers audit reports of high standards. The review involves IRBA re-performing, on a sample basis, certain quality reviews performed by the AGSA's quality reviewers and reporting to the Quality Assurance Committee that makes the final decision of the review. From 2012/13, IRBA will start carrying out a firm-level quality control review in terms of ISQC 1. The arrangement contributes to knowledge transfer in the two Institutions.

## **2. Reportable auditing irregularities**

**3.67 The Auditing Profession Act broadens the obligation of auditors to report “irregularities” by their clients with overall aim of reducing white-collar crime.** Under the predecessor to the Auditing Profession Act — the Public Accountants’ and Auditors’ Act of 1991 — auditors were required to first report “material irregularity” (which was not defined) to management, after which management had 30 days to respond before the regulator (the PAAB) was potentially informed. If the matter was resolved during this time, the auditors filed no report. Under the Auditing Profession Act, if a registered auditor has reason to believe that the management of its client has committed an unlawful act or omission that is likely to cause financial loss, the auditor must, without delay, report the misconduct to IRBA. Within 3 days of submitting its report to IRBA, the auditor must notify management of the report. Within 30 days of having sent the report, the auditor must take reasonable measures to discuss the matter with the management and then send a second report to IRBA, which confirms or dispels the auditor’s initial suspicion. The submission of a report to IRBA has serious consequences for the company’s audit report. Unless the auditor is able to verify that no reportable irregularity had occurred, once a report has been submitted to IRBA, the auditor can no longer issue a “clean” report and the audit opinion must be qualified with a paragraph explaining the reportable irregularity regardless of whether it is resolved and is no longer occurring. At the same time, failure to report a reportable irregularity has potentially serious consequences for the registered auditor: he or she may be found guilty of an offense and fined up to R10 million or imprisoned for a term not exceeding 10 years, or both. IRBA has responsibility under the statute to refer the reportable irregularity to the appropriate regulator, such as, for example, the South Africa Revenue Services, the FSB, CIPC, or the Police Services. That body may, at its discretion, determine whether to conduct a further investigation.

**3.68 Since its establishment in 2006, IRBA has received approximately 5,274 reports of reportable irregularities.** The vast majority of the reports relate to theft, tax issues, and noncompliance with corporate governance requirements. Because the regulator to which IRBA reports the irregularity has no legal obligation to report the disposition of the matter back to IRBA, the outcome and effectiveness of these reports are not easily known. Anecdotal evidence suggests that various stakeholders value this requirement.

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### 3. Auditing investigations and sanctions

**3.69 Under the Auditing Profession Act, IRBA has the authority to investigate and sanction registered auditors for “improper conduct.”** The Disciplinary Rules regarding unprofessional conduct adopted by IRBA provide a long list, which is not intended to be exhaustive, of the types of conduct that can be considered improper. These include, for example, contravention of any law that the auditor is required to follow; failure to respond to a demand from IRBA for documents or the payment of fees or levies; any offence involving dishonesty; failure to perform any work or duties with due care and skill; tax evasion; and personal conduct that is improper, discreditable, unprofessional or dishonorable, or unworthy of a registered auditor or which brings the profession of accountancy into disrepute.

**3.70 The Auditing Profession Act mandates the establishment of a committee to investigate suspected misconduct by registered auditors on behalf of IRBA and recommend to the IRBA Board whether to charge the auditor with improper conduct.** The Investigating Committee operates part-time and is comprised of primarily practicing auditors. It is supported by the IRBA Legal Department, which currently has 5 professionals. The Auditing Profession Act allows IRBA to determine the number and make-up of Committee members. The Investigating Committee should include individuals with significant legal experience. Currently, the Committee has 11 members, comprised of 7 registered auditors, 1 chartered accountant, and 3 lawyers. Ever since the Committee began operations, the chairman has been a registered auditor. The ROSC review team questions whether the independence of the Investigating Committee is compromised due to the majority of members being registered auditors.

**3.71 Investigations may be initiated based on information received from the public, the most common source, or other external entities or garnered by IRBA through inspections and other means.** Once the Investigating Committee receives a referral, it must conduct an investigation. In practice, the staff of the IRBA Legal Department does the underlying work. Although the Auditing Profession Act does not give the Investigating Committee the power to subpoena documents or compel testimony, it does state that the Committee may require that registered auditors provide documents, including audit work papers. The committee frequently requires production of audit working papers and other documents. In 2011, 94 investigations were initiated.

**3.72 Once the Investigating Committee completes its investigation, it submits a recommendation for or against prosecution of the auditor to the Disciplinary Advisory Committee for consideration.** The Disciplinary Advisory Committee is a sub-committee of the IRBA Board which the Board has designated to act on its behalf. If the recommendation is to prosecute, the case must be prosecuted unless it reconsiders this recommendation based on its interaction. Currently, the Disciplinary Advisory Committee is composed of 3 IRBA Board members, 2 of whom are practicing auditors. In the 2011 financial year, the Disciplinary Committee (*para. 3.72*) considered 79 cases and finalized 59 either through settlement or finding that the matter should not be prosecuted. Of the 59 cases finalized, 2 practitioners were admonished, 25 were found guilty by consent (negotiated settlement), and 33 were not prosecuted. The Disciplinary Advisory Committee referred 5 matters to the Disciplinary Committee for prosecution in 2011.

**3.73 The Auditing Profession Act establishes the Disciplinary Committee as the hearing tribunal to adjudicate prosecutions of registered auditors.** The Auditing Profession Act does not fix the number of members for the Disciplinary Committee. The Act does dictate however that the Committee must have as its chair a former judge or senior advocate and that it must include only up to 49 percent registered auditors. The Committee currently includes 11 members, with 4 registered auditors, 5 lawyers and 2 chartered accountants. The majority of cases referred

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to the Disciplinary Committee for prosecution are not related to how an audit is conducted. More often, the cases involve dishonest behavior.

**3.74 Under the Auditing Profession Act, potential sanctions include monetary fines up to R100,000 (US\$ 12,000) per charge, reprimands, suspension of registration, and cancellation of registration.** Whether to publish the name of the sanctioned auditor is within the discretion of IRBA. In most cases, IRBA will publish a description of the charges and sanctions without disclosing the name of the auditor. In 2010, of the 6 cases adjudicated, the auditor's name was published in 3 cases. In 2011, 2 cases were adjudicated and the names were not disclosed to the public in either case. For cases that are settled by consent orders before reaching the Disciplinary Committee, it is the IRBA's policy to not disclose the names of the auditors sanctioned. A ROSC review of the sanctions imposed by either consent order or by the Disciplinary Committee indicates a tendency to levy a relatively small fine on the auditor. Most fines range between R10,000 (US\$ 1,200) and R75,000 (US\$ 9,000). Frequently, some fraction, even half, of the fine is suspended for leniency or on conditions, even with small monetary fines.

**3.75 Although the Auditing Profession Act allows IRBA to exchange confidential information with other regulators, in practice there is little sharing.** While IRBA has positive relationships with other regulators in South Africa, it does not have formal sharing arrangements whereby information relevant to a particular regulator can be passed along as a matter of course. Various regulators within the South African regulatory system such the FSB, the JSE, and the Reserve Bank could benefit from knowing the results of IRBA's inspections and investigations, especially the big four affiliates that audit the vast majority of the entities within the authority of those regulators (e.g., banks, financial service providers, and other JSE-listed companies). The South Africa Revenue Service also could benefit from IRBA-possessed information relating to tax issues. Likewise, information relating to registered auditors that comes into the possession of other regulators during the course of performing their duties could be helpful to IRBA in achieving its mandate.

**3.76 There is frequent interaction during the year between the Reserve Bank's supervision department and the external auditors.** In addition to the statutorily required audit, per the Banks Act and banking regulations, the external auditor is required to report annually on the bank's financial position and results of operations as reflected in the regulatory returns that were submitted by the bank to the Registrar. The Registrar may require that the external auditor perform additional work and may demand access to the audit working papers. Although joint auditors are no longer legally required for banks, all large banks in South Africa continue to have a joint audit.

**3.77 The FSB has a well-designed internal court for disciplinary and sanctioning processes.** While the FSB does not have direct authority to enforce compliance with the Companies Act or accounting standards, it does have authority through its oversight of the JSE to take action against a listed company for material financial misstatements and has used this authority in the past. However, the FSB does not have authority, direct or indirect, to take action against the auditor for misapplication of accounting principles or otherwise. The FSB reports suspected auditor misconduct to IRBA found during an on-site examination or investigation of one of its regulated entities. In addition, FSB is not fully capacitated with experts to review compliance with accounting standards.

#### **4. Accounting Standards — Financial Statements Review**

**3.78 The CIPC has not established a mechanism to review financial statements for compliance with stipulated accounting standards.** In accordance with the provisions of the

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new Companies Act, the CIPC is required to promote the reliability of financial statements by monitoring patterns of compliance with, and contraventions of, financial reporting standards; and making recommendations to the FRSC for amendments to financial reporting standards, in order to secure better reliability and compliance. CIPC is required to establish a system to select and review a sample of financial accountability supplements, audited annual financial statements, or independently reviewed annual financial statements that have been filed in terms of the regulations. However, there is currently a public perception that CIPC is experiencing significant difficulties at the basic operational level of receiving, filing, and making available company returns and information. Until accessibility of company information on a timely basis is improved, there is limited opportunity for CIPC to undertake any sampling to report on compliance with the reporting requirements of the Companies Act. In addition, appropriately qualified staff will need to be recruited if CIPC is to perform such reviews itself.

**3.79 The JSE and SAICA in 2002 formed the GAAP Monitoring Panel—referred now as Financial Reporting Investigation Panel (FRIP)—to review financial statements of listed companies.** The joint initiative was established to fill the gap in the previous Companies Act where there was no requirement to review financial statements for compliance with stipulated accounting standards. The objective of the review process was to contribute toward the production of quality financial reporting of JSE-listed entities: a critical element of a well-functioning market. Salient features of the monitoring process and its transformation are as follows:

- The initial role of the 16-expert GAAP Monitoring Panel was to advise the JSE on alleged cases of noncompliance with financial reporting standards in annual and interim reports and any other company publications on issues brought to its attention through complaints or otherwise – a reactive process.
- In February 2011, the GAAP Monitoring Panel was converted to the FRIP, and JSE started a process of proactively reviewing annual financial statements for IFRS compliance.
- The JSE intends to review every set of financial statements of a listed company at least once within a 5-year cycle. The JSE does this through a partnership with University of Johannesburg using students and academic staff. Approximately 80 listed companies are selected per year for review done using a risk-based approach. Risk areas will change from year to year and from entity to entity.
- Under the new review process, only certain cases where JSE requires detailed technical advice will be referred to FRIP, following a process set out in the FRIP charter to review the case and report to the JSE.
- From 2002 to 2011 the GAAP Monitoring Panel reviewed 44 cases on which it made recommendations to the JSE for corrective action in all but 2 cases. The JSE is able, in its sole discretion, to instruct the management of a noncompliant company to publish or re-issue any information it deems appropriate. In addition, where errors and omissions are identified, the matter is referred to IRBA and SAICA to take the necessary disciplinary action against the member (the accountant or auditor involved in the company).
- From March to December 2011, 56 annual financial statements were proactively reviewed. Sixteen cases were closed either with no comments or with a letter of potential areas of improvement being sent to the issuer. Enquiry letters were written to 40 of the issuers, of which 2 resulted in a further referral to FRIP for advice. By January 2012, 11 of the 40 cases of enquiry were still pending action. The results in Table 3.12 therefore only deal with the 29 closed cases.

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**Table 3.12 Results of JSE review process**

# cases	
2	Annual financial statements needed restatement and public announcement made.
2	Noncompliance such that the JSE agreed to a correction within the next published results.
10	Noncompliance not material this year but will correct in future to avoid potential investor prejudice.
15	Smaller disclosure issues that will be corrected in the future.
<b>29</b>	<b>Closed cases</b>

**3.80 There is no legally mandated institution to conduct reviews of financial statements.** Which institution should be responsible of reviewing financial statements and initiate appropriate remedial actions? Which category of financial statements should be reviewed? These are pertinent questions that Government should address. To enhance the quality of financial statements, the ROSC team supports the view that review of financial statements should be legally mandated, extended beyond the listed companies to other public interest entities, including state-owned entities, and should be conducted by a well-capacitated institution.

#### **IV. ACCOUNTING STANDARDS AS DESIGNED AND PRACTICED**

**4.1** In South Africa, IFRS are the mandatory financial reporting standards. The local requirements on financial reporting by SMEs are also based on the IFRS for SME. Therefore, there is no difference between international standards and local accounting standards.

**4.2 There is generally a high level of compliance with standards in South Africa.** However, there were a few common themes found by the ROSC team in reviews performed by JSE and Ernst and Young<sup>25</sup> that require further strengthening in order to improve the overall quality of financial statements.

- (a) ***There was a “boiler plate” approach to accounting policies.*** The financial statements included a myriad of accounting policies for instruments or transactions not contained in the underlying statements and for matters not affecting the issuer at all. In other instances, where an accounting policy was necessary, the issuer included a generic policy or the preceding year’s policy, without amending it for the specifics of its own business environment or that specific year. In other instances, the accounting policies were silent, leaving the reader guessing as to what the issuer had done. This could be particularly confusing where there was a choice of accounting policy in terms of IFRS or diversity in practice in the application of a specific IFRS standard.
- (b) ***Some financial statements include generic explanations or notes that remain unchanged from year to year.*** Disclosure of information in the previous year is not a

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<sup>25</sup> Each year Ernst & Young offers all listed companies, and state-owned entities, an opportunity to obtain a detailed analysis of how their annual reports are rated against best practice. The annual reports are reviewed using guidelines from the Excellence in Corporate/Integrated Reporting Survey, and a benchmarking report is issued. The report contains practical suggestions and comments that can be used to improve the quality of future reports by the company. In 2012, top-100 companies and top-10 state-owned entities were benchmarked on quality of integrated reports (for the first time).

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sound basis for its repeated inclusion. Incomplete disclosure on related party transactions (IAS 24), financial instruments (IFRS 7), share-based payment (IFRS 2), and business combination (IFRS 3) were also noted.

- (c) The reviews in question also identified challenges of determining fair value in respect to impairments (IAS 16) and loans receivable (IAS 39).

## **V. AUDITING STANDARDS AS DESIGNED AND PRACTICED**

**5.1** In South Africa, ISAs are the mandatory auditing standards. Application of International Standards on Quality Control 1 (ISQC 1) as issued by the IAASB is also mandatory in the country. Therefore, there is no difference between international standards and local auditing requirements.

**5.2 The assessment of compliance with auditing standards is based on the review of work done by the IRBA Inspections Department and comments raised by auditing practitioners.** The main IRBA findings relate to deficiencies in audit documentation because that is the primary focus of inspections. In both its 2011 and 2012 annual reports, IRBA states that the major reason for inspection results not being rated as “satisfactory” related to documentation being insufficient and/or inappropriate. The 2012 report cited the following areas as identified during engagement reviews as having inadequate documentation: fraud and ethical considerations; independence considerations; use of an expert, another auditor, or a service provider; related parties; testing for impairment; carrying value of fixed assets; fair value considerations; and going concern considerations.

**5.3 The small and medium-size practices (SMP) face challenges in keeping up to date with the developments in both accounting and auditing standards.** The small and medium-size practices are required to comply with the stipulated standards and regulators requirements, which they consider to be complex and onerous. While there are a number of capacity-building opportunities offered to small and medium-size practices, especially by SAICA and IRBA, most still face challenges in understanding and applying the evolving standards. In addition, a number of small and medium-size practices expressed concern of losing their revenue base due to the removal of the requirement to conduct an audit for all companies, as provided in the new Companies Act.

## **VI. ISSUES OF SPECIAL INTEREST**

**6.1** There are some special interest issues unique to South Africa, which are discussed in this section.

### **A. Transformation**

**6.2 The aforementioned (Box 3.1) innovative Thuthuka program was established by SAICA to increase the number of Black chartered accountants in South Africa.**<sup>26</sup> One of

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<sup>26</sup> Transformation in the South African context is a strategy to redress the effects of Apartheid, which excluded the majority of the population from participating in the economic activities of the country. Transformation is thus a strategy to ensure that the demographics of each organization reflect the demographics of the population. Emphasis is thus placed on increasing the number of Black (i.e., African Black) accountants in the country, as well as Colored accountants.



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SAICA's prime goals is to strengthen the country's economy by playing a significant and leading role in transformation and skills development. The Thuthuka Education Upliftment Fund (TEUF), a pioneering initiative to promote transformation in the profession, was launched in the Eastern Cape in 2002 and is now a national project. The Thuthuka Bursary Fund program is being offered in 9 of the 13 fully accredited institutions: namely the University of the Witwatersrand; University of Johannesburg; University of Pretoria; Nelson Mandela Metropolitan University; University of Cape Town; Stellenbosch University; University of the Free State; the University of Kwazulu-Natal (Westville); and the North-West University (2012), which will host the undergraduate program at the Mafikeng Campus and the CTA program at the Potchefstroom Campus. It takes a minimum of 7 years for a CA(SA) qualification; and at the end of 2011, 13 CA(SA) qualifiers went through this program. In 2011, a total of 825 students were in this program spread over 8 campuses.

## **B. Integrated Reporting**

**6.3 South Africa is first among countries worldwide to require companies to prepare and issue integrated reports.** In February 2010, the JSE, through its listings requirements, made it compulsory for all listed companies to comply with the King III Code, including the requirement for a company to produce an integrated report for its financial year starting on and after March 1, 2010, or to explain why it was not fulfilling the Code recommendations. In May 2010, the South Africa's Integrated Reporting Committee was established to develop guidelines on good practice in integrated reporting. South Africa's Integrated Reporting Committee was the first in the world to issue draft guidance on a framework for an integrated report when it released its first discussion paper, Framework for Integrated Reporting and the Integrated Report. The International Integrated Reporting Committee referred to this paper when releasing its own discussion paper on a framework in September 2011. The two papers are largely similar. Many JSE-listed companies are now issuing their second or third integrated reports, and their experiences are gathering global attention. This has led to an increase in the amount of social, environmental, and ethical information provided in company reports. Surveys done, especially by the large audit firms, indicate that, even with limited guidance, JSE-listed companies and a number of state-owned entities in South Africa have pro-actively embraced integrated reporting. The levels of application have varied, depending on the maturity and approach by organizations. It is acknowledged that full adoption of integrated reporting is a journey. Therefore, the quality will evolve over the years.

## **C. XBRL**

**6.4 There is growing demand to introduce the use of XBRL in reporting financial information.** The technology, eXtensible Business Reporting Language (XBRL), for the electronic communication of business and financial data provides benefits in the preparation, analysis, and communication of business information. To reduce the administrative requirements and cost and increase greater efficiency, there is growing interest to introduce and require companies to report using XBRL. Increasingly used in many countries around the world, XBRL plays a role in enhancing the data integrity and credibility of financial report and auditing. It facilitates better and faster access to information; transparency in the whole information supply chain is increased. In South Africa, companies are required to prepare and submit separately the same business and financial information in different forms to regulators (JSE, SARS, CIPC, FSB and Reserve Bank), analysts, investors, and other stakeholders, which is onerous and costly. And although several stakeholders have pushed forward the idea to introduce XBRL in South Africa,

the initiative has not taken off. The stakeholders, including the Government, should engage and define a process to implement the XBRL initiative in South Africa.

D. Accountancy Profession in the Public Sector

**6.5 There are only a few professional and technician accountants working in the public sector.** About 4 percent of SAICA members (1,360 of 34,104) work in public sector jobs. Likewise, SAIPA also reports that only a small number of its members work in the public sector. The limited number negatively impacts on the skills available to support financial management roles in public sector entities. In fact, research conducted in 2010 by the National Treasury indicates that vacancy rates for staff in the public sector averaged 31 percent for finance positions, 36 percent for supply chain management, 39 percent for internal audit, and 44 percent for risk management. The situation is made worse by a high turnover rate in public financial management, averaging 14.6 months. Further reports indicate that the skills level and experience of staff appointed to finance departments, especially in relation to the compilation of financial statements that comply with public sector accounting standards, are not adequate. Capacity limitation is one of the causes of consistent poor audit outcomes in the three tiers of government. There are many underlying factors that limit capacity in public sector. The National Treasury’s Capacity Development Strategy for Public Financial Management reports some of the factors, which include organizational and institutional weaknesses, a lack of competent and qualified support staff, and a lack of competitive remuneration. The Auditor General reports that only 13 out of 283 (5 percent) municipalities received clean audit reports for the local government audits covering the 2010/11 financial year. Box 6.1 discusses a unique partnership between the Association of Accounting Technicians (AAT) and SAICA to develop skills necessary for work in the public sector.

Box 6.1 Public Sector Capacity-Building Initiative

a. Association of Accounting Technicians South Africa

SAICA and AAT(SA) entered into a unique partnership to form a sustainable program that develops financial management skills necessary to serve at operational level. The demand from local government was instrumental in establishing the organization. The partnership is dedicated to the education, development, regulation, and support of finance and accounting staff to help them earn the professional respect, recognition and rewards. AAT(SA) offers three professional streams, each aimed at a specific target audience—business, local government, and public sector—and with different qualification levels. Each stream allows mobility from one to the other through additional short programs, if necessary.



Source: [www.aatsa.org.za](http://www.aatsa.org.za)

The business stream focuses on private sector while the local government and public sector streams focus on developing skills required in the public sector. As at June 2012, over 4,000 students had registered for the local government qualifications, of which over 600 were at Local

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Government Accounting Advanced Certificate level. Over 1,800 have already graduated. AAT(SA) enjoys an attendance rate of over 95 percent and a graduation rate of over 60 percent for the Local Government Accounting Certificate. AAT(SA) has finalized development of the qualifications for a Public Sector Certificate in Accounting and Public Sector Advanced Certificate in Accounting and are in the process of enrolling students.

The qualification makes a positive contribution to South Africa's transformation agenda, by developing skills at technician level in the municipalities and providing recognition for those who have developed workplace skills but have not had the opportunity to gain formal qualifications.

#### **b. National Treasury as a registered training office for SAICA**

To contribute in increasing the number of chartered accountants working in public sector, National Treasury has been accredited by SAICA to serve as Registered Training Office with a suitably designated Training Officer. The trainees who register practical training with National Treasury are offered opportunities to work in all the three spheres of Government: national, provincial and local. Currently, there are 23 trainees serving articles in National Treasury.

## **E. King III Code – Corporate Governance**

**6.6 South Africa remains at the forefront in adopting good governance principles that promote an environment of balanced corporate governance.** As follow up to King I (1994) and King II (2002), the King Committee on Corporate Governance released a revised Code and Report on Governance Principles for South Africa (King III) in September 2009, with an effective date of March 1, 2010. The revision was necessitated by the new Companies Act 2008 and changing trends in international governance. King III has broadened the scope of corporate governance in South Africa with its core philosophy revolving around leadership, sustainability, and corporate citizenship. Entities are required to annually report on how it has either positively or negatively affected the economic life of the community in which it operated during the year under review. It recommends that an entity produce an integrated report (in place of an annual financial report) and a separate sustainability report. While King III has no legal backing, except as adopted by the JSE listings requirements, the principles are applicable to all entities (public, private, and non-profit). King III advocates an “apply or explain” approach: an entity can adopt a practice different from that recommended in King III but must explain it.

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## VII. PERCEPTIONS

**7.1 The market perceives accounting graduates from non-accredited universities as less competitive compared to those from accredited universities, leaving the market at a disadvantage.** These students are seen to be receiving a less-competitive education, which hinders their access to funding for studies and jobs. In addition, these universities, mostly located in rural areas, do not offer attractive employment destinations for lecturers, which has a direct effect on learning. These notions negatively impact on the students who come most often from disadvantaged communities. The result is that the potential for developing excellence in accounting is not fully realized. *How should the talent in the non-accredited universities be harnessed?*

**7.2 There is unbalanced compliance in application of accounting standards.** While the current financial statement reviews indicate that generally there is good compliance with the standards on reviewed entities, there is a perception that there are variant applications and levels of compliance especially by small and medium-size enterprises.

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## VIII. POLICY RECOMMENDATIONS

**8.1** The principle-based policy recommendations outlined in this section result from the review and discussions held with stakeholders by the ROSC team. They are formulated on international good practice and take into account the country context. Implementation of the recommendations will contribute to further strengthening of corporate financial reporting practices. To implement the recommendations, the Government and country stakeholders should develop a country action plan that incorporates specific objectives to be undertaken noting the timing (short, medium, or long term) and institution responsible of implementing each action. Commitment from the Government, Steering Committee, and other stakeholders is critical. Development partners should be engaged to support implementation of the action plan with financial and technical assistance. The key policy recommendations focus on enhancing oversight over the professional accountancy bodies with overall aim of increasing access and improving on quality of qualifications, strengthening audit quality reviews, and establishing a legal-backed process of reviewing financial statements and taking corrective sanctions.

### A. Provide Comprehensive Arrangement for Supervision of Accountancy Profession

**8.2** **Appropriate legislation should be enacted to provide for the regulation of both professional accountancy organizations and an audit regulatory body.** While the auditing profession is regulated, there is no national supervision over the professional accountancy bodies. The proposed act should provide the mandate to an institution (regulatory body) that would be responsible for defining and categorizing the education and training (framework) requirements for different accountancy services (e.g., audit, independent review, accounting officers, bookkeepers) and respectively align the PAO qualifications to these categories (i.e., align a PAO qualification to services that members can offer). In addition to promoting qualifications and supporting strengthening all professional accounting organizations, the regulatory body would accredit, register, monitor, and sanction the PAOs: an action that would contribute in developing accountants required to meet the demand in private and public sector. While each PAO would continue to support and regulate its members, the proposed regulatory body should ensure that the education and training offered by professional accountancy organization is appropriate to the types of services being offered by the PAO membership. The regulatory body should have stringent PAO accreditation criteria. The accreditation criteria should take into consideration the Statements of Membership Obligation of IFAC that provide a framework for high-quality accountancy profession. More specifically, these criteria should require PAOs to adopt high-quality membership requirements set in accordance with the IES, and adopt and implement high-level ethics standards such as the IESBA Code of Ethics for Professional Accountants, and establish effective investigation and disciplinary mechanisms. The regulatory body should monitor compliance in accordance with the accreditation criteria on an ongoing basis. This would promote and strengthen the profession and reinforce the supervision of the profession, which is now fragmented among numerous professional accountancy organizations, and would further ensure that providers of different accountancy services are suitably qualified to undertake and provide quality services. The regulatory body should also support promotion of all the qualifications in partnership with the PAOs: an initiative that would increase the visibility of all qualifications to all prospective accountants, employers, tertiary institutions and public. The regulatory body should also promote an initiative, in partnership with PAOs, to ensure most, if not all of, accounting service providers are registered with a PAO to ensure the highest-quality accountancy countrywide. Similar practices have been adopted in Australia and the United Kingdom, which has a Financial Reporting Council.

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**8.3 An independent board should govern the proposed regulatory body with support from a secretariat that has adequate capacity in financial and human resources.** In essence, the regulatory body would continue with the existing IRBA functions in addition to the proposed oversight function over PAOs. In summary, the regulatory body would provide oversight to both accounting and auditing services and promote the provision of the standards, quality, and credibility of financial and non-financial information by entities, including public interest entities. Therefore, it would be prudent to ensure the regulatory body remains independent in its governance and operations—a principle that should be considered when drafting the proposed Accountancy Profession Act. Similarly, to ensure independence, it would be ideal for the regulator to be adequately funded mainly by the Government, although some areas of its operations may be self-funded through, for example, registration fees. The board should operate in an environment of transparency and open consultation with stakeholders and should employ staff who have the competence to carry out the necessary regulatory duties.

## **B. Strengthen Audit Quality Review**

**8.4 The independence of IRBA’s inspection and investigations processes should be strengthened.** IFIAR’s core principles provide that an audit regulator should be “operationally independent,” meaning that it has “the ability to undertake regulatory activity without external interference by those regulated.” The principles further provide that an audit regulator should be “operationally independent...in the exercise of its functions and powers, including not being controlled in its governance by audit practitioners.” While IRBA has a full-time inspections staff and legal department, in reality the most critical decisions regarding IRBA’s monitoring and enforcement programs derive from the Inspections Committee and the Investigating Committee, which are both chaired and otherwise dominated by registered auditors. Take into consideration that the Inspections Committee gave “satisfactory” ratings to 214 out of 218 inspections of public interest entity audits when other more independent audit regulators worldwide are increasingly finding problems in engagement reviews. This fact may suggest a process that is weakened by the lack of independence. In addition, IRBA’s hampered effectiveness from lack of independence is further supported by the fact that the vast majority of investigations undertaken by the Investigating Committee are not related to audit conduct and that the Investigating Committee typically refers only a handful of matters for prosecution each year. These functions should be made fully independent by moving them in-house (within IRBA) with an adequate number of staff with appropriate experience to carry out the responsibilities or, alternatively, the committees should be reconstituted with no registered auditors serving as members. Further, in reference to IFIAR principle, an ethics code should be adopted by IRBA and applied to all employees.

**8.5 The approach, methodology, and rigor of IRBA’s inspections should be strengthened.** IFIAR’s core principles state that “[a]udit regulators should ensure that inspections include effective procedures for both firm-wide and file reviews.” The principles further state that “[t]he inspection process should also include adequate testing of selected audit files in order both to determine the effectiveness of the firm’s quality control system and to assess compliance with applicable laws, rules and professional standards.” IRBA’s current approach to inspections is primarily driven by compliance with audit documentation requirements; there is little testing for compliance with other audit standards and virtually none for accounting standards. Therefore, the following actions should be considered:

- (a) IRBA should strengthen the rigor (and thereby value) of its inspections by reviewing for compliance with all applicable auditing standards.



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- (b) IRBA should reduce its reliance on the firm's internal review of selected audit engagements. Currently, IRBA inspectors will not review half of the engagements they have selected for review if they find that the firm's own internal inspection program is reliable. That approach does not conform to the principle that there should be "adequate testing of selected audit files" by the independent audit regulator.
  - (c) In reference to the IFIAR core principles that state "audit regulators should have a process for assessing risks in the audit environment and audit risks in the individual regulated firms," IRBA should consider developing and performing a more robust risk-analysis when choosing engagements and particular areas within an engagement to review. This may include evaluating current trends and developments affecting audit firms and their clients, monitoring academic research on the auditing profession, and analyzing information derived from public or commercial sources or IRBA's own inspections. This could be enhanced by establishing a research and analysis unit.
  - (d) In order to tackle the more complex areas of an audit during an inspection and be able to challenge the senior audit partners who are typically in charge of such clients, IRBA should raise the level of experience and expertise of its inspection staff. Recently retired audit partners may offer a pool of candidates with the appropriate qualifications. The expertise should be engaged from different sectors.
  - (e) IRBA's existing authority permits it to review for compliance with accounting standards. High-quality auditing and high-quality accountings are both essential to increasing the reliability of financial reporting and protecting the public interest and investors. IRBA should start using its existing authority and review for compliance with applicable accounting standards during inspections.

**8.6 The disciplinary process and sanctioning requires independence, rigor, and timely resolution.** The IRBA Disciplinary Committee should not include practicing auditors, and the monetary penalty available under the law should be increased from its current level of R100,000 (US\$12,000) per charge; new levels should probably align to those of FSB. Names of auditors who are sanctioned through a "settlement order" should be published: an initiative that would serve as a deterrent and also increase the visibility of IRBA. The public has an interest in knowing the names of the auditors that have been found guilty, through consent or otherwise, of misconduct.

**8.7 IRBA resources and capacity should be increased and funding model should be stabilized.** IFIAR's core principles provide that the audit regulator "should have a stable source of funding, which is secure and free from influence by auditors and audit firms and sufficient to execute its powers and responsibilities." The core principles also state that "in order for audit regulators to be effective, it is a prerequisite that there is sufficient staff of appropriate competence." While IRBA is charged with a wide range of responsibilities under the Auditing Profession Act that are both labor and cost-intensive, it does not have adequate financial and human capacity to carry out this mandate. While the move away from charging the firms for inspections on a per-hour basis largely resolved the independence problem, the current model of just relying on the firms to pay for inspections does not seem sustainable. IRBA is in need of additional funding to carry out its existing mandate. To put that additional burden directly on the audit firms, which they will pass on to their clients, would increase pressure on the firms to lower the audit fees in order to keep the total charge from increasing too much. Lowering audit fees often leads auditors to cut corners. While many audit regulators around the world receive a portion of their funding from the audit profession, the Government is often the primary source since the public benefits from audit regulations. Some regulators are funded, in part, through a fee imposed on public companies and other public interest entities under the theory that those entities

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and their shareholders/owners are directly benefiting from the audit regulator's activities. Thus, the Government should consider increasing its funding by looking to the Department of Trade and Industry to make additional contributions.

**8.8 IRBA should be more robust in sharing information with other South Africa regulators.** IFIAR's core principles provide that audit regulators "should make appropriate arrangements for cooperation with other audit regulators and, where relevant, other third parties," such as financial market regulators. The principle goes on to say that "arrangements should be in place for sharing information between audit regulators and other regulators and for protecting the confidentiality of such information." IRBA has the necessary legal authority but in fact does not share information on a regular basis from its inspections or investigatory activities with other South Africa regulators. In practice, IRBA could share inspection findings with other regulators with an interest in the quality of auditing such as the Reserve Bank, the FSB, and the JSE. The procedures for sharing both inspections and investigations information (including an obligation to maintain such information as confidential) should be established through agreed upon memoranda of understanding between IRBA and the individual regulators. The confidentiality and sensitivity of information should be considered before deciding what to disclose.

**8.9 The follow-up process of reportable irregularities should be improved to ensure corrective actions are taken.** While conceptually the requirement for auditors (and independent reviewers) to submit reportable irregularities is considered a valuable tool for detecting and deterring wrongdoing, there should be an obligation on the part of the regulator to take appropriate follow-up action on the reported irregularity. In addition, that regulator should be required to report back to IRBA or CIPC (as applicable) on an annual basis as to the dispositions of the reports so that outcomes may be measured. The concept of materiality should be introduced into the reporting requirement arising out of fraud or theft to allow for the efficient use of resources. Finally, the required second report should allow for more flexibility as sometimes it is not possible for an auditor (or independent reviewer), due to circumstances beyond their control, to make a determination as to the state of the irregularity within the short deadline currently imposed.

## **C. Establish a legally backed review of financial statements**

**8.10 The proposed legislation to regulate both professional accountancy organizations and an audit regulator (paragraph 8.2) should require review of financial statements of large public interest entities for compliance with financial reporting standards.** The requirement should be applicable to companies with a public interest score above a certain limit and state-owned entities. Therefore, a unit/division within the recommended regulatory body should be responsible of conducting reviews for compliance with reporting standards, and take appropriate actions for noncompliant companies. The unit/division should be capacitated with adequate financial and qualified human resources. In addition, the unit/division should develop detailed operating procedures and sanctions based on both international good practice and the experience of the FRIP and the JSE to ensure timely reviews and punitive sanction processes. Options of transferring the work and mechanics of FRIP to the new institution should be considered. The institution should enter into memoranda of understanding with IRBA, the JSE, the CIPC, and other regulatory bodies concerned with financial reporting to allow sharing of information. In particular, based on the shared information, CIPC would be able to report to the Minister of Trade and Industry on trends in compliance with financial reporting standards, as required by Companies Act. It could also provide input to the FRSC on recommended changes and improvements to financial reporting standards.

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## **D. Broaden Professional Education and Training**

**8.11 All professional accountancy organizations should increase their partnership engagement with universities and other tertiary institutions.** To increase the number of accountants in the country, professional accountancy organizations should promote their qualification to be offered in partnership with tertiary institutions. The tertiary institutions should increase awareness for opportunities and entry options in the accounting and auditing sector, both private and public.

**8.12 Professional accountancy organizations and tertiary institutions, where appropriate, should include public sector modules in their education and training curricula.** To address the training needs and capacity shortage in the public sector, it is imperative for the professional accountancy organizations and tertiary institutions (in partnership with Government) to start or increase the inclusion of public sectors modules in their curriculum and create incentives to motivate both students and the providers.

## **E. Strengthen Financial Reporting Standards Council**

**8.13 The FRSC should be provided with necessary infrastructure and resources to achieve its mandate.** DTI should provide the council with resources – financial and adequate and suitably qualified support staff – necessary to meet its mandate.

## **F. Strengthen Professional Accountancy Organizations**

**8.14 All professional accountancy organizations should be strengthened to have capacity to increase and serve their members.** With the appropriate capacity, professional accountancy organizations are able to further public interest; develop capable and competent accountancy professionals; promote and enforce strong professional and ethical standards; and act as a resource to government, regulators, and other stakeholders. Except for SAICA and SAIPA, all other professional accountancy organizations in South Africa should strengthen their capacity to promote their brand, develop more members to serve both public and private sectors, increase their value offering to their members, and institutionalize strong governance structures and processes. Promotion of PAO brands contributes to improving the relevance in the market. The professional accountancy organizations should aspire to meet IFAC Statement of Membership Obligations within the scope of their responsibility for difference SMO areas. The value offering will assist the members in delivering high-quality services in both private and public sectors.

## **G. Introduce limited liability partnerships**

**8.15 South Africa should consider enacting a law that would allow audit firms to organize as limited liability partnerships (LLPs).** In the recent past, the accountancy profession in South Africa has started to explore alternative organizational forms that confer limited liability; contrary to the unlimited liability which exposes partners' personal assets to the risk of litigation. Historically, the practicing accountants in various countries have lobbied hard for legislation that limits their exposure to unlimited litigation awards through formation of LLPs. Since the early 1990s, United States, United Kingdom, Germany, India, Singapore and many

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other countries have passed legislation allowing their audit firms to become LLPs. In an LLP, the personal assets of an audit firm's non-negligent partners are protected in the event of a lawsuit against a negligent partner. However, the LLP legislation does not provide for protection of the assets of the audit firm or the personal assets of negligent partners. Because the LLP audit firms may continue to face a significant threat from liability, South Africa may consider requiring the firms and audit practitioners to carry a sufficient level of professional indemnity insurance. This would enhance protection for both the auditors and potential claimants. The Government should analyze the experiences from other countries that allow LLP before deciding on an ultimate structure.

## **H. Make Information Accessible to Public**

**8.16 Large private companies with public interest should be required to make available their audited financial statements to the public on request.** Therefore, the recommendation by CIPC to the Minister of Trade and Industry to restrict public access to audited financial statements to public companies only should not be adopted. Some private companies are accountable to the public through a combination of their economic significance and social responsibility. Therefore, to enhance transparency of information, audited financial information of such companies, with a public interest score above 1,000, should be made available to the public on request.

## **I. Strengthen Small and Medium-Size Practitioners**

**8.17 SMPs should be encouraged to strengthen their resources and capabilities in order to be competitive in providing professional services.** All accounting firms, including the SMPs, need to put in place more robust procedures for meeting the challenges of complying with heightened standards of professional conduct, and complex requirements of international accounting and auditing standards. From this perspective, the SMPs that want to be competitive in the market place need to raise their professional capabilities through expansion. It is worth noting that if an accounting firm does not have a viable size, it is very difficult for that firm to continuously support enhancement of professional capabilities. Merger of a number of SMPs and/or networking with a regional/international network of accounting firms may be the most effective vehicle for SMP expansion in South Africa. The SMPs should also give more thoughts on how else they could strengthen their resources and capabilities, and how they could focus on alternative service offerings in niche and high value-creating areas. In this regard, they should make reference to the tools and resources of the IFAC SMP Committee, available free of charge on the IFAC website.



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