

Exposure Draft
November 2009
Comments are requested by 31 March 2010



**Rules Regarding Improper Conduct and
Code of Professional Conduct for
Registered Auditors**

REQUEST FOR COMMENTS

The Committee for Auditor Ethics (CFAE) and the Independent Regulatory Board for Auditors (IRBA) approved the release of the exposure draft, *Rules Regarding Improper Conduct* and the *Code of Professional Conduct for Registered Auditors (the Code)* for publication in November 2009. To ensure that all relevant stakeholders are consulted and to streamline the consultation process, interested and affected stakeholders are invited to submit **written** comments to the IRBA. The Committee for Auditor Ethics (CFAE) will consider comments received on the proposed Code prior to adoption of the final Code. All comments received will be regarded as being on public record unless confidentiality is requested.

Please submit written comments, preferably by e-mail, or on a computer disk to:

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Copies of this exposure draft may be downloaded free-of-charge from the IRBA website at <http://www.irba.co.za>

The mission of the IRBA is to endeavour to protect the financial interests of the South African public and international investors in South Africa through the effective and appropriate regulation of audits conducted by registered auditors, in accordance with internationally recognised standards and processes.

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**EXPOSURE DRAFT: CODE OF PROFESSIONAL CONDUCT
FOR REGISTERED AUDITORS**

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EXPLANATORY MEMORANDUM

1. Introduction

This memorandum provides background to, and an explanation of the exposure draft *Rules Regarding Improper Conduct* (the *Rules*) and the *Code of Professional Conduct for Registered Auditors* (the *Code*), approved for exposure by the Committee for Auditor Ethics (CFAE) and the Board in November 2009.

In line with the Independent Regulatory Board's (IRBA's) legislative mandate, the IRBA's objectives are to create the framework and principles to contribute to the protection of members of the public who rely on the services of registered auditors, and to support registered auditors who carry out their duties competently, fearlessly and in good faith. The goal is to help create an ethical, value-driven financial sector that encourages investment and confidence and promotes sound practices by developing and maintaining ethical standards which are internationally comparable.

The proposed Rules and Code will replace the existing "*Old Disciplinary Rules - Rules 2.1.1 to 2.1.21 (the Old Disciplinary Rules)*" and the "*IRBA Code*" and discharges the responsibilities of the CFAE contained in section 21 of the Auditing Profession Act, No. 26 of 2005 (the Act), to *determine what constitutes improper conduct by registered auditors and by developing requirements and guidelines for professional ethics, including a code of professional conduct.*

The CFAE welcomes comments on these *Rules* and the *Code*.

Comments should be received by 31 March 2010.

2. Background

Section 20 of the Act empowers the IRBA to establish the CFAE. The functions of the CFAE are specified in section 21 of the Act, which requires the CFAE to assist the IRBA to:

- Determine what constitutes improper conduct by registered auditors by developing requirements and guidelines for professional ethics, including a code of professional conduct;
- Interact on any matter relating to its functions and powers with professional bodies and any other body or organ of state with an interest in the auditing profession; and
- Provide advice to registered auditors on matters of professional ethics and conduct.

The CFAE determined the following as guiding principles to be followed in the revision of the existing *Old Disciplinary Rules* and *IRBA Code*:

- Raising awareness of ethical behaviour.
- Promoting ethical behaviour and discouraging unethical behaviour.
- Facilitating social integration.
- Providing guidance on ethical decision-making.

The CFAE recognises that trust is the underlying core value in the relationship between the auditors and their clients and other stakeholders. The Proposed Code and Rules seek to enhance the trustworthiness of the auditing profession and motivated the revision of the existing *Old Disciplinary Rules* and *IRBA Code*.

3. Adoption of Revised IFAC Code of Ethics (2009)

After careful consideration and the completion of a mapping exercise between the existing *IRBA Code* to the *Revised IFAC Code of Ethics for Professional Accountants (July 2009)* (the *Revised IFAC Code*) published by the International Federation of Accountants (IFAC), the CFAE has determined that it is appropriate for the IRBA to adopt *Parts A and B, and the related Definitions*, contained in the *Revised IFAC Code* in their entirety, as these relate to professional services provided by registered auditors (as defined). Part C of the *Revised IFAC Code* has not been adopted as it provides for ethical conduct of Professional Accountants in Business.

IFAC's copyright permissions policy permits modifications to the *IFAC Code* to accommodate jurisdictional requirements in different countries. Consequently, more stringent requirements in the existing *IRBA Code* are incorporated into the relevant sections in Parts A and B of the *Code*. References to "*professional accountants*" in the *IFAC Code* have been replaced throughout with a reference to "*registered auditors*" (as defined) as the IRBA only regulates registered auditors. All such modifications are reflected by *underlining and italics*.

The "*Old Disciplinary Rules*" setting out what constitutes Improper Conduct by, and Punishment for, a registered auditor have been revised and are exposed for comment here as the "*Rules Regarding Improper Conduct*".

The CFAE decision to adopt the parts of the IFAC Code indicated was based on the outcome of the mapping exercise and the following considerations:

- 3.1 The G20 Finance Ministers and Central Bank Governors (of which South Africa is a member body) has recommended worldwide convergence of auditing and accounting standards. The International Ethics Standards Board (the IESBA) of IFAC has similarly urged professional bodies and regulators of accountants and auditors worldwide to adopt the *Revised IFAC Code*, modified as necessary for jurisdictional requirements. The adoption of the *Revised IFAC Code* aligns with the statutory responsibilities of the IRBA to develop standards that are internationally comparable, and supports the commitment of the auditing profession in South Africa to ensure that the South African economy continues to participate in the global marketplace as a highly respected player.
- 3.2 The *Revised IFAC Code* embodies years of intellectual capital of the auditing and accounting profession in its development with input from the auditing profession and broader public around the world. It represents a significant effort by IFAC to enhance the credibility of the auditing and accounting profession around the world as it codifies very high standards of ethical behaviour expected to be applied.
- 3.3 South Africa has a long history of working with IFAC in the development of auditing, accounting and ethics standards. South Africa was represented on the IESBA and Task Groups working on the development of the *Revised IFAC Code* which reflects this ongoing commitment and enabled the perspectives of the auditing profession in South Africa to be considered by the IESBA during the drafting of the *Revised IFAC Code*.
- 3.4 The preamble to the existing IRBA Code indicates that the present IFAC Code of Ethics, adopted by the South African Institute of Chartered Accountants (SAICA) with effect from January 2003, "*will provide useful guidance to registered auditors*". Consequently registered auditors have, since January 2003, been familiar with the conceptual framework regarding threats and safeguards contained in the IFAC Code.

- 3.5 The International Auditing and Assurance Standards are underpinned by the requirement for auditors using those standards to comply with the IFAC Code. As a consequence of the Board adopting the ISAs as the standards to be applied in South Africa from January 2005, registered auditors are already familiar with the conceptual framework regarding threats and safeguards contained in the IFAC Code.

4. Drafting conventions

Conceptual framework

Part A of the *Code* establishes the fundamental principles of professional ethics for registered auditors and provides a conceptual framework for complying with those principles. Part B of the *Code* describes how the conceptual framework is to be applied in specific situations. In all cases, the objective to be achieved, as outlined in the conceptual framework, is for the registered auditor to comply with the fundamental principles. In doing so, the registered auditor will either take the actions prescribed in the *Code* to address the circumstance or relationship described in the *Code* that creates a threat to compliance with the fundamental principles or, when the *Code* does not address the specific circumstance or relationship, identify and evaluate threats to compliance with the fundamental principles. If the threats are not at an acceptable level, apply safeguards to eliminate the threats or reduce them to an acceptable level.

Modifications to the Revised IFAC Code

- 4.1 The *Status of the Code* and *Joint and Vicarious Liability* provisions contained in the existing *IRBA Code* have been retained, and are slightly modified to accommodate the adoption of the *Revised IFAC Code*.
- 4.2 The term “professional accountants” in the Revised IFAC Code has been replaced throughout with a reference to “*registered auditors*” as the IRBA regulates only individual registered auditors and their firms (as defined) in the *Code* and the Act.
- 4.3 The *Code* identifies a requirement by use of the word “*shall*” and thus brings the language in the Code in line with that adopted by the IAASB in the ISAs for identifying “*Requirements*” in individual ISAs. Provisions in the existing *IRBA Code* that are intended to convey requirements often used the word “should” and have been replaced with the word “shall” where such requirements have been incorporated into the Code. The revised Code requires registered auditors to comply with all provisions denoted by the word “shall,” unless compliance is prohibited by law or regulation or an exception is permitted by the Code.
- 4.4 The changes to the IFAC Code to address perceptions that in many instances the term “*consider*” could be seen by some as being less robust than intended accommodates the more stringent provisions in the existing changes to the Code and is consistent with the following principles of drafting:
- “*Consider*” will be used where the accountant is required to think about several matters;
 - “*Evaluate*” will be used when the accountant has to assess and weigh the significance of a matter; and
 - “*Determine*” will be used when the accountant has to conclude and make a decision.

These conventions are consistent with the definitions of those words found in standard dictionaries.

- 4.5 New definitions, modifications to definitions in the *Revised IFAC Code* and definitions retained from the existing *IRBA Code* have been added to

accommodate more stringent South African requirements or regulatory requirements in the *Code* including:

- Act;
- Board;
- Client;
- Client account;
- Client monies;
- Director or officer;
- Firm;
- Professional services;
- Professional; and
- Registered auditor and a registered auditor in public practice.

4.6 Specific requirements from the existing *IRBA Code* have been incorporated into the following sections of the *Code*:

- Part A: sections 130, 140 and 150;
- Part B: sections 210, 240, 250 and 270;
- Part B: section 290: Modifications to paragraphs: 290.106, 290.114, 290.116, 290.121, 290.122, 290.151, 290.155, 290.213, 290.220, 290.222 and 290.502; and
- Part B: section 291: Modifications to paragraphs 291.109, 291.116 and 291.117.

Modifications to the Rules Regarding Improper Conduct

4.7 The *Rules* now incorporate Definitions pertaining to terms used therein as they will stand as a separate section in the IRBA Manual of Information, preceding the *Code*.

4.8 Improper conduct now includes: “without reasonable cause or excuse, failure to comply with:

4.8.1 Any Auditing Pronouncements prescribed by the Board; and

4.8.2 Any of the provisions of the *Code*. Footnotes in the *Code* are regarded as an integral part of the *Code* for the purposes of the *Rules*.

4.9 References to “*accountant*” are deleted as the *Rules* now apply only to *registered auditors* (as defined) in the Act and as contained in the provisions of the *Code*.

5. Effective Date

The effective date of implementation of the *Code* is still to be determined. Comments received in this regard will be considered by the CFAE in determining the effective date.

6. Guide for Commentators

The CFAE welcomes comments on the proposed revisions. Comments are most helpful when they refer to specific paragraphs, include the reason for the comments and, where appropriate, make specific suggestions for any proposed changes to wording to enable the CFAE to fully appreciate the respondent’s position. Where a respondent agrees with proposals in the exposure draft (especially those calling for a change in current practice), it will be helpful for the CFAE to be made aware of this view.

RULES REGARDING IMPROPER CONDUCT

These Rules Regarding Improper Conduct (“**these Rules**”) repeal and replace the “Old” Disciplinary Rules 2.1 to 2.1.21 referred to in section 59(8)(c). These Rules are prescribed by the Board under section 4(1)(c) <from the effective date¹>.

1. Definitions

- 1.1. In these Rules, the terms below have the meanings assigned to them -
- 1.1.1 “**Act**” means the Auditing Profession Act, No. 26 of 2005 and any expression used in these Rules which is defined in the Act bears, unless the context indicates the contrary, the meaning assigned to it in the Act;
- 1.1.2 “**Board**” means the Independent Regulatory Board for Auditors established in terms of section 3;
- 1.1.3 “**Code**” means the Code of Professional Conduct prescribed by the Board under section 4(1)(c);
- 1.1.4 “**firm**”, in the context of these Rules, means:
- (a) A firm registered with the Board as a registered auditor in terms of section 38 including:
 - (i) partnerships of which all partners are themselves registered auditors;
 - (ii) sole proprietors where the proprietor is a registered auditor; and
 - (iii) a company incorporated and registered under the Companies Act that complies with section 38(3) of the Act and inter alia, where only individuals who are registered auditors are shareholders, where every shareholder is a director and every director is a shareholder;
 - (b) An entity that controls such parties, through ownership, management or other means; and
 - (c) An entity controlled by such parties, through ownership, management or other means.
- 1.1.5 “**professional services**” in the context of these Rules means services requiring accountancy or related skills performed by a registered auditor including accounting, auditing, taxation, management consulting and financial management services. These are regarded as relating to, but not limited to:
- (a) *Audit and other assurance services:*
 - (i) Financial statement audit and reviews, other assurance services such as regulatory reporting, sustainability and performance reporting;
 - (ii) Company accounting advisory services such as preparation of accounting records and financial statements in accordance with recognised financial reporting standards and applicable statutes; and
 - (iii) Company statutory services;

¹ To be determined post exposure for public comment

- (b) *Taxation services:*
 - (i) Tax return preparation, tax calculations for the purpose of preparing accounting entries, tax planning and other tax advisory services, and assistance in the resolution of tax disputes relating to corporate tax, indirect tax and international tax matters;
- (c) *Advisory services:*
 - (i) Accounting advisory and financial management advisory services: accounting support, conversion services for new and revised accounting standards, financial modeling and project management;
 - (ii) Business performance services: business effectiveness, people and change management, operational and business finance;
 - (iii) Internal audit: risk and compliance services, review and monitoring of internal controls, risk management, compliance services, corporate governance and audit committee advisory services;
 - (iv) Corporate finance services: mergers and acquisitions, valuations, infrastructure financing, debt and capital markets - due diligence reviews, transaction services and designated advisor services to listed companies;
 - (v) Corporate recovery services: liquidation and insolvency administration, curator bonis, administration of deceased estates, judicial management and trusteeships;
 - (vi) Financial risk management services: actuarial services, banking and risk advisory, regulatory and compliance services, technical accounting;
 - (vii) IT Advisory: security, privacy and continuity, enterprise resource planning; information system audit services, IT project advisory, governance and performance;
 - (viii) Forensic services: dispute advisory, ethics and integrity monitoring, fraud risk management, intellectual property and other investigations and regulatory compliance.

1.1.6 “**registered auditor**”, in the context of these Rules, means an individual or firm registered as an auditor with the Board;

1.1.7 “**registered auditor in public practice**”, in the context of these Rules, means a registered auditor that provides professional services as defined above.

1.1.8 “**these Rules**” means the Rules Regarding Improper Conduct prescribed under section 10(1) and includes these definitions; and

1.2. Any reference to any section in these Rules is a reference to the corresponding section in the Act;

1.3. These Rules shall, wherever possible, be construed in conformity with the Act; and

1.4. The headings to and any footnote in these Rules shall be taken into account in the interpretation of these Rules.

2. Improper Conduct

The Board is obliged by section 48 to investigate and deal with any complaint, charge or allegation of improper conduct against a registered auditor which may be laid before it, and is empowered to impose any of the prescribed sanctions set out in section 51(3) and Disciplinary Rule 8.1 and 8.2, in respect of any improper conduct. While the acts or omissions specified in the following paragraphs are not intended to be a complete list of acts or omissions which could constitute improper conduct on the part of a registered auditor and which are punishable in accordance with the provisions of the Act and Disciplinary Rules, a registered auditor shall be guilty of improper conduct if such registered auditor –

- 2.1 contravenes or fails to comply with any provision of the Act with which it is their duty to comply;
- 2.2 contravenes or fails to comply with any provision of any other Act with which it is their duty to comply in their capacity as registered auditor to an entity or in providing professional services;
- 2.3 commits any offence involving dishonesty, and in particular (but without prejudice to the generality of the foregoing) theft, fraud, forgery or uttering a forged document, perjury, bribery or corruption;
- 2.4 is dishonest in the performance of any work or duties devolving upon them in relation to –
 - 2.4.1 any professional services or duties by a registered auditor; or
 - 2.4.2 any office of trust which they have undertaken or accepted;
- 2.5 without reasonable cause or excuse, fails to comply with any Auditing Pronouncements prescribed by the Board;
- 2.6 without reasonable cause or excuse, contravenes or fails to observe any of the requirements of the Code;
- 2.7 without reasonable cause or excuse, fails to perform any professional services or duties with such a degree of professional competence, due care and skill as in the opinion of the Board may reasonably be expected, or fails to perform the professional services or duties at all;
- 2.8 with intent to evade or to assist any other person to evade any tax, duty, levy or rate whatsoever (whether the same be payable to the Government or to a provincial government or to a local authority or to any other body or authority in the Republic) –
 - 2.8.1 knowingly or recklessly prepares or makes, or assists any other person to prepare or make, any false statement (whether such statement be oral or in writing); or
 - 2.8.2 signs any false statement in relation thereto recklessly or knowing it to be false; or
 - 2.8.3 knowingly or recklessly prepares or maintains any false books of accounts or other records;
- 2.9 permits their name to be used in connection with any estimate of earnings contingent upon future transactions in a manner which may lead to the belief that they vouch for the accuracy of the estimate;
- 2.10 seeks, either before or during the period of training of a trainee accountant, to impose any restraint whatever on the trainee accountant concerned which will apply after the date of termination of the training period, or threatens or attempts

to enforce any such restraints after such date. The provisions of this rule will not, however, apply so as to prohibit a registered auditor from seeking to restrain a trainee accountant, for a period of not longer than one year from the date of the trainee's ceasing to be employed by the registered auditor, from soliciting for professional services from an existing client of that registered auditor or from accepting an engagement of any kind from an existing client of that registered auditor;

- 2.11 directly or indirectly stipulates or receives from a trainee accountant who is or has been serving under a training contract, or from any other person, any payment, reward, compensation or consideration for agreeing to the cancellation of such training contract - provided that it shall not be deemed a breach of this rule if a registered auditor requires to be or is reimbursed in respect of disbursements actually made by them to the Board in connection with a training contract which is subsequently cancelled, and of which disbursements they are able to produce proof to the satisfaction of the Board;
- 2.12 without reasonable cause or excuse, fails to answer or to deal with appropriately within a reasonable time any correspondence or other communication from the Board or any other person which reasonably requires a reply or other response;
- 2.13 without reasonable cause or excuse, fails to comply within a reasonable time with an order, requirement or request of the Board;
- 2.14 without reasonable cause or excuse, fails to resign from a professional appointment when requested by the client to do so;
- 2.15 without reasonable cause or excuse, fails after demand to pay any subscription or any fee, levy or other charge payable to the Board;
- 2.16 abandons their public practice without previous notice to their clients and without arranging with the clients for the despatch of the clients' business or the care of the clients' property in their possession or under their control; or
- 2.17 without reasonable cause or excuse, conducts himself or herself in a manner which tends to bring the auditing profession into disrepute.

