

24 February 2012  
(Ref: CVW/IRBA Stand)

Independent Regulatory Board for Auditors (IRBA)  
Director of Standards

For Attention: Sandy van Esch

Dear Sir/Madam

**RE: COMMENTS ON DRAFT ASSURANCE STANDARDS FOR AUDITORS BY ABVA  
TECHNICAL COMMITTEE**

## **1. EXISTING BEE VERIFICATION INDUSTRY**

### **Observation**

- 1.1 We understand that the draft assurance standard's intention is only to deal with the standards applicable to registered auditors and that it is not applicable to SANAS accredited Verification Agencies. The Dti's Verification Manual gazetted on 18 July 2008 is applicable only to the SANAS Verification Agencies whilst it is only a "guideline" for Registered Auditors. We however believe that once these standards are approved it will create an expectation that the existing BBBEE Verification Industry will also have to adhere to them. Should such a dispensation become compulsory for the existing industry, it would also be contrary to the Dti and the IRBA's commitment to the ABVA board to develop a less onerous dispensation to accommodate the existing industry.
- 1.2 We believe that having two different sets of Verification/Assurance Standards would not only confuse the market but would lead to an anti-competitive industry. Application of the IRBA standard only in its current format would create a significant challenge to the existing BBBEE Verification Industry as these Verification Agencies would effectively be expected to become Registered Audit Firms which would also be contrary to the Dti and the IRBA's commitment to the ABVA board to develop a less onerous dispensation to accommodate the existing industry.
- 1.3 The contexts of the comment above is that the majority of verification agencies' accreditation with SANAS will be expiring from February 2013. That is one year from the date of this commentary. SANAS, whether on the instructions of the Dti or out of own accord, have been refusing to accept any further applications for accreditation or for the extension of scope of accreditation for any of the existing verification agencies. This means that the only avenue left for any business other than an auditing firm to become a verification professional and for the existing industry to continue trading after February 2013 would be to apply for approval through the IRBA route. It takes time to develop standards such as yours and ABVA's concern is that



1

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the timeframes we are dealing with as outlined above will be insufficient to hash up a different standard for non-auditors. This would be counterproductive to the intended purpose of creating capacity to service businesses that want to be verified. We believe that if the Dti, Treasury and the IRBA have not managed to accommodate existing SANAS Verification Agencies by way of appropriate amendments to the Auditing Profession Act and the Assurance Standard applicable to BBEE certification, by February 2013 it would have a significant impact on the capacity in the BBEE verification industry and in turn on the ability of treasury to fulfil its obligations in terms of the PPPFA. In addition, it could lead to the demise of an industry created by the Dti and the resulting implications thereof.

#### **Suggestion**

We suggest that the future of SANAS accredited Verification Agencies be clarified in as far as whether and if so how they will be accommodated by IRBA in their capacity as Verification Professional Regulator. In addition we suggest that the assurance standard must make the application of the Dti's Verification Manual compulsory if it is going to remain compulsory for the current BBEE Verification Agencies.

## **2. DISTINCTION BETWEEN LIMITED AND REASONABLE ASSURANCE:**

### **Observation**

- 2.1 The document expressly states that materiality is not the basis for determining the level of assurance. It is left to the measured entity to elect what level of assurance should be applied. On the other hand the draft standards seem to imply that the level of assurance is something the auditor should decide on given both the inherent risk of the engagement as well as the audience that will be relying on such a certificate. The BBEE status certificate is a public document that is valid for a year. There will therefore be no control over who the intended users are. They will be from different categories including the private sector, government, tender boards, other verification professionals that need to rely on them etc. The risk and impact of the use will therefore differ from user to user. When planning the engagement and when issuing the certificate the Registered Auditor cannot be expected to know who will be relying thereon or that it will only be used for a specific category of user during the 12 month validity period. Consequently it cannot be pre-determined what the level of reliance would be on the certificate or the magnitude of the decisions made based on that certificate.
- 2.2 There is therefore a pervasive and overarching risk that an inappropriate level of assurance may be relied upon for a particular application. This risk in our view is always material. Furthermore we believe this risk to be ever present.
- 2.3 We believe that as the Auditor is obliged to have regard to the intended users he cannot come to a different conclusion but to insist on 'reasonable assurance' given the potential wide usage of the certificate.



- 2.4 A measured entity may elect to obtain a limited assurance certificate. During the validity period of a year a customer or Tender Board may insist on a reasonable assurance certificate. This would result in the measured entity having to obtain two certificates during the same period.
- 2.5 Furthermore the procurement officers understanding of the meaning of the respective levels of assurance and secondly the appropriate application thereof is not necessarily adequate and in all likelihood won't be as they are not auditors.
- 2.6 A fractional difference in score on any of the elements can be material as it could lead to a difference in BBEE status level. This risk is prevalent from the beginning of the engagement and once again the auditor can come to no other conclusion but that reasonable assurance should be the basis for the engagement.
- 2.7 We believe that the distinction between level 2 and up and level 3 and down in deciding on the level of assurance is inappropriate as decision making and the contribution by a measured entity to a customer's procurement scorecard may be material at any BBEE status level. Firstly in many cases one would not know what the level of the business is before the engagement is complete. The use of the BEE status level in determining the level of assurance is therefore circular. Secondly, one could rightly ask why make the distinction at that level and not for example say between Level 7 and 8. This distinction between limited and reasonable assurance confirms that one can place less reliance on the one type of assurance than on the other.
- 2.8 One of the factors listed to take into consideration is whether the business will tender for government business. In many cases this risk is no greater than that for private sector tenders/procurement. The abovementioned criteria implies that tender boards and procurement officers understand the distinction between limited and reasonable assurance and that they will place more reliance on the one or the other. Our concern with this assumption is twofold:
- 2.8.1 Tender boards operate in accordance with the PPPF Act and its regulations. If the PPPF Act and its regulations do not provide for a higher weight to be attached to the one above the other and for a mechanism of weighing the one above the other— absolute reliance will be places on both or alternatively reliance on the two types of assurance levels would be inconsistent from the one board to the other. The proposed distinction between limited and reasonable assurance would therefore imply that the PPPF Act or its regulations



may need to be amended to ensure consistent and appropriate application thereof.

- 2.8.2 Officials on tender boards often do not have auditing qualifications. The understanding and ability to distinguish between limited and reasonable assurance would therefore be lacking. In addition, as the decision as to which level of assurance should be obtained lies with the Measured Entity, a BBEE certificate may be supported by an inappropriate or insufficient level of assurance.
- 2.9 The reliance that a measured entity can place on a suppliers' limited assurance certificate can be material in itself. For example a measured entity can have one supplier that is a level 4 and it procures significant amounts from that supplier insofar that it's (the suppliers) certificate will be material to the measured entity's BBEE status level. If the measured entity believes that it requires a reasonable level of assurance due to the material impact that the supplier's BBEE status has on it's own scorecard, then it would be inappropriate to rely on the limited assurance certificate of its supplier, both for the measured entity and it's BBEE auditor.
- 2.10 The BBEE Act Amendment Bill imposes significant fines (maximum of 10% of turnover) should a measured entity be found guilty of misrepresentation or fronting. The BBEE auditor faces an equally severe penalty for an offence. We believe that corporate SA will probably enforce reasonable assurance on their supply chain in any event. For a considerable period of time until government issued a directive in this regard in February 2010, non-accredited consulting businesses issued scorecards and sometimes even certificates that in many cases were accepted as sufficient and appropriate evidence of the BEE status of a measured entity. The SANAS Accredited Verification Agencies provided a higher level of assurance, however a lesser level of assurance was acceptable until such time as government was compelled to legislate that only certificates from accredited verification agencies would be acceptable proof of a measured entity's BBEE status. It is not necessary to repeat the same mistakes of the past. Only one level of assurance will be appropriate.

### **Suggestion**

We suggest that all engagements and certificates are performed on the basis of a reasonable assurance. We further suggest that where there is not sufficient appropriate evidence the verification professional should simply not allocate points instead of a expressing a qualified conclusion.



### 3. ANTI COMPETITIVE NOTIONS

#### Observation

- 3.1 The draft SASAE3502 suggests that it would be more beneficial for the incumbent financial auditor to also do the BBBEE certification, i.e. that a person / firm that has done the audit will already have the required knowledge of the business / control environment. Sanas R47 specifically prohibits the current industry from suggesting that the verification will be quicker, easier and cheaper if a certain consultant prepares the scorecard and supporting file. We believe that IRBA should ensure that it is perceived as independent and does not favor or is biased towards the registered auditors *vis a vis* verification industry, especially given that the IRBA will regulate verification professionals from outside the auditing profession as well.
- 3.2 The application of the verification manual is currently mandatory in terms of the Codes. The draft standard refers to it as 'guidance'. We believe that the application of two sets of assurance "standards" would lead to double standards being applied between the existing industry and the auditors during the transitional period. The Codes currently makes the application of the Verification Manual compulsory for all verification professionals. Draft SASAE3502 cannot avoid this by merely referring to the Verification Manual as appropriate 'guidance'. Where legislation compels the application thereof, as it currently does, it is compulsory for approved auditors and accredited verification agencies alike to apply it.
- 3.3 It is important to ensure at all stages of the expansion / development of this industry, that there is no unfair competition by one party over another. The conditions for joining and staying within the industry should be uniform and equitable for all players. Having two sets of codes of conduct, manuals, management system requirements, etc with certain clauses lighter or more strict on one set than on the other opens up the possibility for unfair competition.

#### Suggestion

We suggest that any reference to the BBBEE verification being incorporated into the financial audit be removed from the draft standard (also refer to our comments below on Independence). In addition we suggest that no reference is made to the BBBEE verification being easier, faster or better if it is performed by the incumbent financial auditor. We also suggest that all reference to the Verification Manual being merely 'guidance' be replaced with clear direction that its application is mandatory.



#### **4. INDEPENDENCE**

##### **Observation**

- 4.1 It is assumed that there is no conflict of interest in doing both the financial audit and the BEE verification of the same entity. We believe this is not necessarily the case. By way of example: If an auditing firm has a significant audit client of for example R1.2 mil in fees and is then engaged to perform the BEE verification as well, being provided by the client with an expected score of level 2 for example. We believe that the auditing firm will be very reluctant to inform the client that it is actually non-compliant, should that be the case - fearing that it could potentially not only lose the verification but also the financial auditing business.
- 4.2 We believe this threat to the independence of the auditor to be pervasive, ever present and therefore material.

##### **Suggestion**

In our view there is a conflict of interest in the event of the financial audit and the BBBEE certification being performed by the same auditor. We suggest that this conflict be incorporated in the statement.

#### **5. ANCILLARY MATTERS**

##### **Observation**

- 5.1 The draft statement does not contain any reference to a process to deal with complaints and appeals with regard to the certificates issued neither with regard to a process on how registered auditors will inform the public of any withdrawal of certificates.
- 5.2 The example scorecards in Appendix A3 do not contain a total score for all elements and neither is the scorecard translated into a BEE status level.
- 5.3 There is no column for actual achievement in the suggested scorecards. In other words it contains columns for the applicable weighting, targets and ultimate score but not for the numerator nor denominator and percentage achievement against target for the particular measurement. This information is required when the scorecard needs to be consolidated into a group scorecard, in particular when another auditor / verification agency performed the certification.
- 5.4 Disclosure of Ownership in scorecard should include a statement as to whether any of the following has been applied in the calculation of ownership:
1. Continued Consequence principle: yes/no and % ownership/points arising therefrom;
  2. Use of Modified Flow through: yes/no



**3. Mandated Investments: Included/Excluded**

The above information is required for “downstream” ownership calculations.

- 5.5 We suggest that the certificate indicates the measurement period and “as at” measurement date.
- 5.6 The document uses the term measurement date to refer to verification date. This is not appropriate. The term measurement date is not defined yet in the legislation and the inappropriate use of the term could lead to some unintended interpretation problems with the Enterprise Development and Socio Economic Development elements.
- 5.8 Requirements for verifying EME’s is overly cumbersome. The turnover thresholds can be determined with reference to other external evidence such as affidavits, bank statements, VAT returns etc. The suggestions in the assurance standard will increase the cost of these verifications where it is exactly intended that this constituency of businesses should not be prejudiced.

Yours faithfully

**ASSOCIATION OF BEE VERIFICATION AGENCIES**

Per:



**CHRIS VAN WYK**  
Chairperson

