

PROPOSED IRBA STAFF AUDIT PRACTICE ALERT 5: THE AUDITOR'S CONSIDERATIONS  
WITH RESPECT TO TRANSACTIONS THAT ARE NOT AT ARM'S LENGTH

**STAFF AUDIT PRACTICE ALERT 5**

June 2020



**THE AUDITOR'S CONSIDERATIONS WITH RESPECT TO TRANSACTIONS THAT ARE  
NOT AT ARM'S LENGTH**

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**This publication is not meant to be exhaustive.** Reading this publication is not a substitute for reading the abovementioned pronouncements, as they are the authoritative texts.

The perpetration of fraud, causing material misstatements in the financial statements and/or non-compliance with laws and regulations, has become more prevalent at entities in South Africa over the past few years. Registered auditors (auditors) are required to be alert to the possibility of fraud thereby enabling them to respond appropriately. Due to this prevalence, auditors have called for guidance regarding the auditor's considerations with respect to transactions that are not at arm's length. Consequently, the IRBA has responded to the needs on the auditor's considerations relating to transactions that are not at arm's length.

This IRBA Staff Audit Practice Alert, therefore, serves to provide auditors with guidance and considerations to be made with respect to transactions that are not at arm's length, and the possible auditor's responses to the resulting audit risks.

**INTRODUCTION**

The International Standard on Auditing (ISA) 315 (Revised), *Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and its Environment* (ISA 315), deals with the auditor's responsibility to identify and assess the risks of material misstatement in the financial statements.

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1. Transactions that are not at arm's length may pose risks in an audit of the financial statements, because if such transactions are not identified by management and/or the auditor it could give rise to risks that are not addressed in the audit, and ultimately in misstatements in the financial statements.
2. ISA 200 deals with the overall objectives of the auditor in conducting an audit of the financial statements,<sup>1</sup> including obtaining sufficient appropriate audit evidence to reduce audit risk to an acceptably low level.<sup>2</sup> Audit risk is a function of the risks of material misstatement and detection risk.<sup>3</sup> ISA 200 explains that the risks of material misstatement may exist at two levels:<sup>4</sup> the overall financial statement level and the assertion level for classes of transactions, account balances and disclosures.
3. Risks at the financial statement level relate pervasively to the financial statements as a whole and potentially affect many assertions. Risks of material misstatement at the assertion level consist of two components: inherent risk and control risk.
  - *Inherent risk* is described as the susceptibility of an assertion about a class of transaction, account balance or disclosure to a misstatement that could be material, either individually or when aggregated with other misstatements, before consideration of any related controls.
  - *Control risk* is described as the risk that a misstatement that could occur in an assertion about a class of transaction, account balance or disclosure and that could be material, either individually or when aggregated with other misstatements, will not be prevented or detected and corrected on a timely basis by the entity's system of internal control.
4. The auditor's risk identification and assessment process is iterative and dynamic. The auditor's understanding of the entity and its environment, the applicable financial reporting framework, and the entity's system of internal control are interdependent concepts within the requirements to identify and assess the risks of material misstatement. In obtaining the understanding required by ISA 315, initial expectations of risks may be developed and be further refined as the auditor progresses through the risk identification and assessment process. In addition, ISA 315 and ISA 330<sup>5</sup> require the auditor to revise the risk assessments, as well as modify further overall responses and further audit procedures, based on audit evidence obtained from performing further audit procedures in accordance with ISA 330, or if new information is obtained.
5. Risks of material misstatement identified and assessed by the auditor include both those due to error and fraud. Although both are addressed by ISA 315, the significance of fraud is such that further requirements and guidance are included in ISA 240<sup>6</sup> in relation to risk assessment

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<sup>1</sup> ISA 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing*.

<sup>2</sup> ISA 200, paragraph 17.

<sup>3</sup> ISA 200, paragraph 13(c).

<sup>4</sup> ISA 200, paragraph A36.

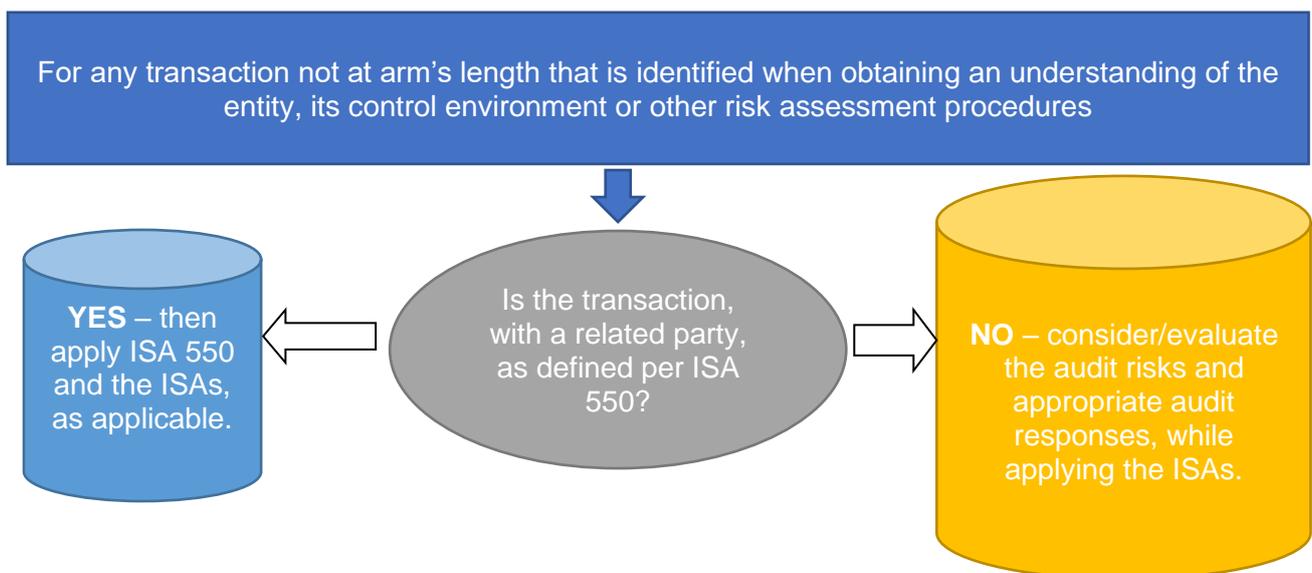
<sup>5</sup> ISA 330, *The Auditor's Responses to Assessed Risks*.

<sup>6</sup> ISA 240, *The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements*.

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procedures and related activities to obtain information that is used to identify, assess and respond to the risks of material misstatement due to fraud.

6. Further, fraud is defined in ISA 240 as an intentional act, by one or more individuals among management, those charged with governance, employees or third parties, involving the use of deception to obtain an unjust or illegal advantage.<sup>7</sup>
7. Although fraud is a broad legal concept, for the purposes of the ISAs, the auditor is concerned with fraud that causes a material misstatement in the financial statements. Two types of intentional misstatements are relevant to the auditor – misstatements resulting from fraudulent financial reporting and misstatements resulting from the misappropriation of assets. Although the auditor may suspect or, in rare cases, identify the occurrence of fraud, the auditor does not make legal determinations of whether fraud has actually occurred.<sup>8</sup> Refer to the following IRBA alert for a detailed discussion on fraud: [www.irba.co.za](http://www.irba.co.za)
8. The following decision making process is useful when any transaction not at arm's length has been identified:



### *Risk Assessment Procedures*

9. The auditor shall perform risk assessment procedures to provide a basis for the identification and assessment of risks of material misstatement at the financial statement and assertion levels. Risk assessment procedures by themselves, however, do not provide sufficient appropriate audit evidence on which to base the audit opinion.<sup>9</sup>

<sup>7</sup> ISA 240, paragraph 12(a).

<sup>8</sup> ISA 240, paragraph 3.

<sup>9</sup> ISA 315, paragraph 5.

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10. The risk assessment procedures shall include the following:
- (a) Inquiries of management, of appropriate individuals within the internal audit function (if the function exists) and of others within the entity who in the auditor's judgment may have information that is likely to assist in identifying risks of material misstatement due to fraud or error.
  - (b) Analytical procedures
  - (c) Observation and inspection.<sup>10</sup>

*Transactions that are not at arm's length*

11. Flowing from risk assessment procedures, an arm's length transaction is defined in ISA 550<sup>11</sup> as a transaction conducted on such terms and conditions as between a willing buyer and a willing seller who are unrelated and are acting independently of each other and pursuing their own best interests.<sup>12</sup>
12. The focus of this IRBA alert is on identifying transactions that are not at arm's length, and does not focus on parties that are related. The table below, which is not exhaustive, lists possible indicators of transactions that are not at arm's length during the audit.<sup>13</sup>

<p><b>Significant Involvement of Family Members</b></p> <ul style="list-style-type: none"> <li> Family members involved with the entity may not be identified due to changes in surnames through marriage or by deeds registry which may result in difficulties in identifying family members in third or fourth generation businesses.</li> </ul>
<p><b>Trust Arrangements</b></p> <ul style="list-style-type: none"> <li> Trustees or beneficiaries may not be identified, and transactions with them may not be identified.</li> <li> Controlling parties not known.</li> </ul>
<p><b>Those Charged with Governance Sensitive to Disclosures</b></p> <ul style="list-style-type: none"> <li> Sensitivity to the disclosure of the identity of other businesses that are trading or transacting with the entity.</li> <li> Sensitivity to the disclosure of loans by or to the entity on favourable terms.</li> </ul>
<p><b>Transactions with No Readily Ascertainable Market Value</b></p> <ul style="list-style-type: none"> <li> Purchase or sale of assets not at arm's length.</li> <li> Services rendered by family members/other parties who are familiar with the entity, such as consultancy, secretarial, design, decorating or gardening services.</li> </ul>

<sup>10</sup> ISA 315, paragraph 6.

<sup>11</sup> Please refer to Appendix B for a Summary of Definitions of a Related Party, per IFRS, Companies Act, JSE Listings Requirements, National Treasury, King IV, Income Tax Act, 1962 and the Reference to Related Entities in the IRBA Code

<sup>12</sup> ISA 550, *Related Parties*, paragraph 10(a).

<sup>13</sup> These indicators were adopted from an Institute of Chartered Accountants in England and Wales (ICAEW) publication, *The Audit of Related Parties in Practice* (2010).

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<ul style="list-style-type: none"><li>✚ Free gifts or services to friends.</li><li>✚ Broad-Based Black Economic Empowerment (B-BBEE) fronting.</li></ul>
<b>Business Property Trading</b> <ul style="list-style-type: none"><li>✚ Owner rents or buys property below market rates.</li><li>✚ Entity rents or buys property from owner at above market rates.</li><li>✚ Entity buys land or buildings, surplus to requirements, to accommodate the owner or a related party.</li></ul>
<b>Inappropriate Approval Process</b> <ul style="list-style-type: none"><li>✚ Transaction(s) not approved.</li><li>✚ Transaction(s) that have not been subject to the required appropriate approval process.</li><li>✚ Management override of controls/process.</li><li>✚ Breakdowns identified through internal audit reports and other reports.</li></ul>
<b>Loans</b> <ul style="list-style-type: none"><li>✚ Loans at nil or reduced rates of interest.</li><li>✚ Provision of unsecured loans or preferential security.</li><li>✚ Drawings by directors, as if the entity were a partnership.</li><li>✚ Continual roll-over of loans with no repayment.</li><li>✚ Inadequate or no documentation supporting loans.</li><li>✚ Additional loans granted despite the business having cash flow problems.</li><li>✚ Transactions not disclosed.</li><li>✚ Loans that are not straightforward, such as loans to employees, on unusually favourable terms.</li><li>✚ Significant cash outflows being expensed inappropriately.</li></ul>
<b>Joint Ventures</b> <ul style="list-style-type: none"><li>✚ Overly complex joint venture arrangements, particularly where the business rationale is unclear.</li><li>✚ Special purpose vehicles used for financing arrangements.</li></ul>
<b>Management Charges and Management Services</b> <ul style="list-style-type: none"><li>✚ The value received for management charges is difficult to establish, which could arise from funds being moved around the group.</li><li>✚ Employees appearing to work for the entity not on the payroll, and employees on the payroll not appearing to work for the entity.</li><li>✚ Management charges to or from other entities.</li></ul>
<b>Unknown Business Relationships</b> <ul style="list-style-type: none"><li>✚ Discussions at board or management meetings include references to unknown</li></ul>

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<p>parties.</p> <ul style="list-style-type: none"> <li> Relationships identified from minutes of those charged with governance/annual general meetings.</li> </ul>
<p><b>Entertainment Costs</b></p> <ul style="list-style-type: none"> <li> Unusually high levels of entertainment expense for the nature of the business in which the entity is involved.</li> </ul>
<p><b>Collusive Relationships with Business Contacts</b></p> <ul style="list-style-type: none"> <li> Change of suppliers without a tendering process, or to less favourable terms and conditions.</li> <li> Customers taken on without normal credit checks.</li> <li> Unusual levels of activity with certain suppliers or customers.</li> <li> No clear business rationale for unusually large discounts.</li> </ul>
<p><b>Limited Documentation</b></p> <ul style="list-style-type: none"> <li> Limited documentation supporting lease agreements.</li> <li> Inadequate documentation of agreements or a lack of clear business rationale.</li> <li> Transactions without explanation or supporting documentation.</li> </ul>
<p><b>Share Ownership</b></p> <ul style="list-style-type: none"> <li> Complex equity transactions and restructurings without a clear business rationale.</li> </ul>
<p><b>Suspense Accounts</b></p> <ul style="list-style-type: none"> <li> Long-standing uncleared items and a failure to investigate.</li> <li> Offsetting entries in suspense accounts to expense accounts.</li> <li> Difficulties in reconciling inter-company balances.</li> <li> Entries in suspense accounts made to make inter-company accounts balance.</li> </ul>
<p><b>Going Concern</b></p> <ul style="list-style-type: none"> <li> Economic pressure in entity's industry.</li> <li> Entity experiencing cash flow or liquidity pressures.</li> </ul>
<p><b>Many Group Auditors</b></p> <ul style="list-style-type: none"> <li> Unclear rationale for splitting the group audit between two or more firms.</li> </ul>

13. The above factors are also possible indicators of the existence of related parties.
14. ISA 330 requires the auditor to design and implement overall responses to address the assessed risks of material misstatement at the financial statement level.<sup>14</sup> In addition, ISA 330 further explains that the auditor's assessment of the risks of material misstatement at the financial statement level, together with the auditor's overall responses, is affected by the auditor's understanding of the control environment. ISA 330 also requires the auditor to design

<sup>14</sup> ISA 330, paragraph 5.

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and perform further audit procedures whose nature, timing and extent are based on and responsive to the assessed risks of material misstatement at the assertion level.<sup>15</sup> The auditor may consider the illustrative procedures in Appendix A for purposes of risk assessment and further procedures resulting from transactions entered into by the entity that are not at arm's length.

**Questions to be considered to determine the audit implications of transactions that are not at arm's length**

15. In consideration of and in response to the "questions to be considered", the auditor is guided by the requirements and application material contained in the relevant ISAs.
16. It is also important to note that the ISAs state that the auditor shall plan and perform an audit with professional scepticism, recognising that circumstances exist that cause the financial statements to be materially misstated.<sup>16</sup>
17. Once the transactions that are not at arm's length have been identified as per paragraph 12, the questions to be considered, as set out in the table below, can be used by the auditor when considering the audit implications of transactions that are not at arm's length.

<b>Audit Considerations/Questions to be Considered</b>	<b>Applicable References</b>
Have you obtained an understanding of the control environment relevant to the audit?	ISA 315, paragraph 12
Have you considered overall audit responses to address the assessed risks of material misstatement at the financial statement level? (For example, going concern, incentives to management, etc.)	ISA 330, paragraphs 5 and A1
Have you obtained an understanding of non-compliance with laws and regulations relevant to the audit?	ISA 250, <i>Consideration of Laws and Regulations in an Audit of Financial Statements (ISA 250)</i> ; Non-Compliance with Laws and Regulations, per the IRBA Code of Professional Conduct for Registered Auditors (Revised November 2018) (IRBA Code (Revised November 2018))
Has the transaction undergone the appropriate approval process within the entity?	ISA 500, <i>Audit Evidence</i>

<sup>15</sup> ISA 330, paragraph 6.

<sup>16</sup> ISA 200, paragraph 15.

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Have you made enquiries of personnel within the entity, other than management?	ISA 315, paragraph 6(a)
Is the transaction(s) an industry practice/norm?	ISA 315
Have you evaluated the business rationale (or the lack thereof) for the transaction?	ISA 240, paragraph 33(c)
Have you considered the need to use the work of a management expert?	ISA 500, paragraph 8
Have you considered the need to use an auditor's expert, where relevant?	ISA 620, <i>Using the Work of an Auditor's Expert</i> , paragraph 5
Have you considered economic pressures on the entity's management?	ISA 240
Have you considered going concern pressures?	ISA 570, <i>Going Concern</i>
Have you considered whether there is any publicly available negative media coverage in respect of the entity, such as SENS announcements?	
Have you considered confirming the terms of the transaction(s) with the counterparty?	ISA 505, <i>External Confirmations</i>
Have you considered your reporting responsibilities with regard to non-compliance with laws and regulations?	ISA 250; Non-Compliance with Laws and Regulations, per the IRBA Code (Revised 2018); Financial Intelligence Centre Act (2001)
Do you have procedures to identify and report reportable irregularities as required by the Auditing Profession Act?	<i>Revised Guide for Registered Auditors: Reportable Irregularities in terms of the Auditing Profession Act</i> , Auditing Profession Act; Non-Compliance with Laws and Regulations
Have you considered the possible impact of the existence of transactions that are not at arm's length in forming an opinion on the financial statements?	ISA 450, <i>Evaluation of misstatements identified during the audit</i> ISA 700, <i>Forming an opinion and reporting on financial statements</i>

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18. The above table is not an exhaustive list of considerations and should not detract from the requirements of the audit engagement team to exercise its professional judgement. Appendix A provides illustrative procedures at the assertion level.

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**Appendix A**

**Illustrative Procedures which may be used for risk assessment and further procedures for transactions with the entity that might not be at arm's length**

<b>Illustrative Procedures (this is not an exhaustive list)</b>	
1	Determine and evaluate the entity's process (including relevant controls), if any, for authorising, identifying and accounting for transactions. Document the assessment as to whether or not significant transactions would be identified by the process.
2	Determine and evaluate the entity's process, if any, for prohibiting individual directors or other members of management from exercising significant influence over transactions in which that person is a related party.
3	Obtain from management personnel (or prepare) a list of all related parties and compare it with the previous year's list and the shareholder's records. Where a related party does not appear in the current year, consider the existence of transaction(s) that are not at arm's length with that party.
4	Distribute to the audit team the list of parties from the previous year that are no longer listed as related parties by the entity's management in the current financial period for possible identification of any transaction(s) that is/are not at arm's length.
5	Consider obtaining representation from the entity's management as to the existence of significant or unusual transactions (including transactions that are not at arm's length). Where the auditor is a component auditor, management representation may be obtained from the parent entity's management as well.
6	If applicable, consider enquiring of predecessor auditors, or other firms involved in the audit, as to their knowledge of transactions that may not be at arm's length.
7	Document any affiliations that the directors or senior management have with other entities, as a possible trigger to identify any transaction(s) that are not at arm's length.
8	Inquire of appropriate management personnel and other finance staff whether there were any transactions that were not conducted at arm's length.
9	Perform procedures to identify additional significant, unusual, or non-recurring, transactions that may not be at arm's length. Such procedures could include: <ul style="list-style-type: none"> <li>(a) Identifying major customers, suppliers, borrowers and lenders; and significant changes to these relationships.</li> <li>(b) Inspecting lawyer/attorney billings.</li> <li>(c) Inspecting bank guarantees.</li> <li>(d) Inspecting contract awards.</li> <li>(e) A review of overdue receivables or payables.</li> <li>(f) Inspecting investment transactions.</li> </ul>

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	<ul style="list-style-type: none"> <li>(g) Transactions at, or near, the year-end.</li> <li>(h) A review of transactions with unusual terms of trade.</li> <li>(i) Considering where related parties may have occurred but not been charged, or circumstances have not changed.</li> <li>(j) Inspecting returns by the entity to regulatory authorities.</li> <li>(k) Inspecting shareholders' registers to identify significant shareholders.</li> <li>(l) Inspecting contracts and agreements with key management and directors.</li> <li>(m) Inspecting contracts and agreements with other entities that have directors in common.</li> <li>(n) Inspecting specific invoices and correspondence from the entity's professional advisers (perhaps in respect of the sale of the entity's assets).</li> <li>(o) Inspecting significant contracts and agreements outside the entity's normal course of business.</li> <li>(p) Inspecting agreements for the provision of services to certain parties under terms and conditions that are outside the entity's normal course of business.</li> <li>(q) Inspecting relationships of guarantees and guarantor.</li> <li>(r) Reviewing/inspecting minutes of board meetings/annual general meetings.</li> </ul>
10	<p>Where parties have been identified, and with whom transactions that are not at arm's length occurred, prepare (or obtain) a schedule or a summary, where appropriate, and obtain an understanding of the business purpose of the transaction(s).</p> <ul style="list-style-type: none"> <li>(a) Examine invoices, agreements, etc.</li> <li>(b) Examine the approval of the transaction both by management and shareholders.</li> <li>(c) Obtain confirmation of any outstanding balances.</li> <li>(d) Obtain information as to the financial standing of the parties regarding meeting their obligations.</li> <li>(e) Indicate whether disclosure is required or not.</li> <li>(f) Agree with management or those charged with governance.</li> </ul>
11	<p>Where it is still uncertain whether the transaction is at arm's length or not, consider:</p> <ul style="list-style-type: none"> <li>(a) Obtaining confirmation of significant information directly from third parties.</li> <li>(b) Obtaining further information and references on suppliers or customers.</li> </ul>

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## Appendix B

### Summary of Definitions of a Related Party, per the ISAs, IFRS, Companies Act, JSE Listings Requirements, National Treasury, King IV, Income Tax Act, 1962 and the Reference to Related Entities in the IRBA Code

#### **ISA 550, Related Parties**

1. ISA 550 defines a related party as a party that is either:
  - A related party as defined in the applicable financial reporting framework; or
  - Where the applicable financial reporting framework establishes minimal or no related party requirements:
    - a) A person or other entity that has control or significant influence, directly or indirectly through one or more intermediaries, over the reporting entity;
    - b) Another entity over which the reporting entity has control or significant influence, directly or indirectly through one or more intermediaries; or
    - c) Another entity that is under common control with the reporting entity through having:
      - i. Common controlling ownership;
      - ii. Owners who are close family members; or
      - iii. Common key management.

However, entities that are under common control by a state (that is, a national, regional or local government) are not considered related, unless they engage in significant transactions or share resources to a significant extent with one another.<sup>17</sup>

#### **IAS 24, Related Party Disclosure**

2. Where an entity is required to comply with International Financial Reporting Standards (IFRS) as the applicable financial reporting framework, the relevant standard to refer to is International Accounting Standard (IAS) 24, *Related Party Disclosure*.
3. IAS 24 defines a related party as a person or entity that is related to the entity that is preparing its financial statements (in this Standard referred to as the "reporting entity").
  - a) A person or a close member of that person's family is related to a reporting entity, if that person:
    - i. has control or joint control of the reporting entity;
    - ii. has significant influence over the reporting entity; or

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<sup>17</sup> ISA 550, paragraph 10(b).

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- iii. is a member of the key management personnel of the reporting entity or of a parent of the reporting entity.
- b) An entity is related to a reporting entity, if any of the following conditions applies:
  - i. The entity and the reporting entity are members of the same group (which means that each parent, subsidiary and fellow subsidiary is related to the others).
  - ii. One entity is an associate or joint venture of the other entity (or an associate or joint venture of a member of a group of which the other entity is a member).
  - iii. Both entities are joint ventures of the same third party.
  - iv. One entity is a joint venture of a third entity and the other entity is an associate of the third entity.
  - v. The entity is a post-employment benefit plan for the benefit of employees of either the reporting entity or an entity related to the reporting entity. If the reporting entity is itself such a plan, the sponsoring employers are also related to the reporting entity.
  - vi. The entity is controlled or jointly controlled by a person identified in point (a).
  - vii. A person identified in point a(i) has significant influence over the entity or is a member of the key management personnel of the entity (or of a parent of the entity).
  - viii. The entity or any member of a group of which it is a part provides key management personnel services to the reporting entity or to the parent of the reporting entity.<sup>18</sup>
- 4. IAS 24 further defines a related party transaction as a transfer of resources, services or obligations between a reporting entity and a related party, regardless of whether a price is charged.<sup>19</sup>
- 5. IAS 24 also defines close members of the family of a person as those family members who may be expected to influence, or be influenced by, that person in their dealings with the entity and include:
  - a) That person's children and spouse or domestic partner;
  - b) Children of that person's spouse or domestic partner; and
  - c) Dependants of that person or that person's spouse or domestic partner.<sup>20</sup>

**Companies Act**

- 6. The South African Companies Act, 2008 (Act No. 71 of 2008) (Companies Act) defines related and inter-related persons and control as (1):
  - a) An individual is related to another individual, if they –
    - i. are married, or live together in a relationship similar to a marriage; or

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<sup>18</sup> IAS 24, paragraphs 9(a) & (b).

<sup>19</sup> IAS 24, paragraph 9.

<sup>20</sup> IAS 24, paragraph 9.

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- ii. are separated by no more than two degrees of natural or adopted consanguinity of affinity;
  - b) An individual is related to a juristic person, if the individual directly or indirectly controls the juristic person, as determined in accordance with subsection (2); and
  - c) A juristic person is related to another juristic person, if –
    - i. either of them directly or indirectly controls the other, or the business of the other, as determined in accordance with subsection (2);
    - ii. either is a subsidiary of the other; or
    - iii. a person directly or indirectly controls each of them, or the business of each of them, as determined in accordance with subsection (2).
- (2) For the purposes of subsection (1), a person controls a juristic person, or its business, if:
- a) In the case of a juristic person that is a company:
    - i. that juristic person is a subsidiary of that first person, as determined in accordance with Section 3(1)(a); or
    - ii. that first person, together with any related or inter-related person, is:
      - A. directly or indirectly able to exercise or control the exercise of the majority of the voting rights associated with securities of that company, whether pursuant to a shareholder agreement or otherwise; or
      - B. has the right to appoint or elect, or control the appointment or election of, directors of that company who control a majority of the votes at a meeting of the board.
  - b) In the case of a juristic person that is a close corporation, that first person owns the majority of the members' interest, or controls directly, or has the right to control, the majority of members' votes in the close corporation;
  - c) In the case of a juristic person that is a trust, that first person has the ability to control the majority of the votes of the trustees, or to appoint the majority of the trustees, or to appoint or change the majority of the beneficiaries of the trust; or
  - d) That first person has the ability to materially influence the policy of the juristic person in a manner comparable to a person who, in ordinary commercial practice, would be able to exercise an element of control referred to in paragraphs (a), (b) and (c).
- (3) With respect to any particular matter arising in terms of this Act, a court, the Companies Tribunal or the Panel may exempt any person from the application of a provision of this Act that would apply to that person because of a relationship contemplated in subsection (1) if the person can show that, in respect of that particular, there is sufficient evidence to conclude that the person acts independently of any related or inter-related person.

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***JSE Listing Requirements***

7. The JSE Listings Requirements define a related party in paragraph 10.1 (b) as:
- i. A material shareholder;
  - ii. Any person that is, or within the 12 months preceding the date of the transaction was, a director of the issuer or its holding company. For the purpose of this definition, a director includes a person that is, or within the 12 months preceding the date of the transaction was, not a director, but in accordance with whose directions or instructions the directors are or were accustomed to act;
  - iii. Any adviser to the issuer that has, or within the 12 months preceding the date of the transaction had, a beneficial interest, whether direct or indirect, in the listed company or any of its associates;
  - iv. Any person that is, or within the 12 months preceding the date of the transaction was, a principal executive officer of the issuer, by whatever position he may be, or may have been, designated and whether or not he is, or was, a director;
  - v. The asset manager or management company of a property entity, including anyone whose assets they manage or administer;
  - vi. The controlling shareholder of the persons in paragraph 10.1 (b) (v); and
  - vii. An associate of the persons in paragraph 10.1 (b) (i) to (vi) above.

Notwithstanding the above definitions, the JSE may, in its sole discretion, determine that a transaction is a related party transaction, if extraordinary conditions exist.

***National Treasury's Accounting Manual for Departments***

8. In the public sector, National Treasury's Accounting Manual for Departments, *Related Party Disclosures*, defines a related party as a person or an entity with the ability to control or jointly control the other party or exercise significant influence over the other party, or vice versa; or an entity that is subject to common control, or joint control. Further, the following are regarded as related parties of the reporting department:
- a) A person or a close member of that person's family is related to the department, if that person:
    - i. has control over the department; or
    - ii. is a member of the management of the department or its executive authority.
  - b) An entity is related to the department, if any of the following conditions apply:
    - i. the entity is a member of the same economic entity (which means that each controlling entity, controlled entity and fellow controlled entity is related to the others) or group entity;
    - ii. the entity is controlled or jointly controlled by a person identified in (a); and

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- iii. a person or a close member of that person's family who has control over the department has significant influence over that entity or is a member of the management of that entity (or its controlling entity).

**King IV Report on Governance for South Africa 2016**

- 9. King IV defines a related party as a person or entity as set out in Section 2(1) of the Companies Act. It applies mutatis mutandis to organisations other than companies.

**South African Income Tax Act No. 58 of 1962 (Income Tax Act, 1962) – Definition of “connected person”**

- 10. Section 1 of the Income Act, 1962 states that a “connected person” means:
  - (a) in relation to a natural person—
    - (i) any relative; and
    - (ii) any trust (other than a portfolio of a collective investment scheme) of which such natural person or such relative is a beneficiary;
  - (b) in relation to a trust (other than a portfolio of a collective investment scheme)—
    - (i) any beneficiary of such trust; and
    - (ii) any connected person in relation to such beneficiary;
  - (bA) in relation to a connected person in relation to a trust (other than a portfolio of a collective investment scheme), any other person who is a connected person in relation to such trust;
  - (c) in relation to a member of any partnership or foreign partnership—
    - (i) any other member; and
    - (ii) any connected person in relation to any member of such partnership or foreign partnership;
  - (d) in relation to a company—
    - (i) any other company that would be part of the same group of companies as that company if the expression “at least 70 per cent of the equity shares in” in paragraphs (a) and (b) of the definition of “group of companies” in this section were replaced by the expression “more than 50 per cent of the equity shares or voting rights in”;
    - (ii) . . . . .
    - (iii) . . . . .
    - (iv) any person, other than a company as defined in section 1 of the Companies Act that individually or jointly with any connected person in relation to that person, holds, directly or indirectly, at least 20 per cent of—
      - (aa) the equity shares in the company; or
      - (bb) the voting rights in the company;
    - (v) any other company if at least 20 per cent of the equity shares or voting rights in the company are held by that other company, and no holder of shares holds the majority voting rights in the company;
    - (vA) any other company if such other company is managed or controlled by—
      - (aa) any person who or which is a connected person in relation to such company; or
      - (bb) any person who or which is a connected person in relation to a person contemplated in item (aa); and
    - (vi) where such company is a close corporation—

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- (aa) any member;
- (bb) any relative of such member or any trust (other than a portfolio of a collective investment scheme) which is a connected person in relation to such member;  
and
- (cc) any other close corporation or company which is a connected person in relation to—
  - (i) any member contemplated in item (aa); or
  - (ii) the relative or trust contemplated in item (bb); and
- (e) in relation to any person who is a connected person in relation to any other person in terms of the foregoing provisions of this definition, such other person:  
Provided that for the purposes of this definition, a company includes a portfolio of a collective investment scheme.

***IRBA Code (Revised November 2018) – Reference to Related Entities***

11. The IRBA Code refers to related entities in paragraph R400.20 as follows: “As defined, an audit client that is a listed entity includes all of its related entities. For all other entities, references to an audit client in this Part include related entities over which the client has direct or indirect control. When the audit team knows, or has reason to believe, that a relationship or circumstance involving any other related entity of the client is relevant to the evaluation of the firm’s independence from the client, the audit team shall include that related entity when identifying, evaluating and addressing threats to independence.”<sup>21</sup>

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<sup>21</sup> IRBA Code (Revised November 2018), paragraph R400.20.