

Proposed Amendment

May 2016

Comments requested by 30 June 2016



Proposed Amendment to the Code of Professional Conduct for Registered Auditors Custody of Client Assets

REQUEST FOR COMMENTS

The Independent Regulatory Board for Auditors' (IRBA) Committee for Auditor Ethics (CFAE) approved the proposed amendment to Section 270.4 of the *Code of Professional Conduct for Registered Auditors* (the IRBA Code) in November 2015 for exposure for a period of 30 days. A Board Notice to the same effect will be published in the Government Gazette for public comment. The proposed amendment might be modified in light of comments received before being issued in its final form.

The IRBA adopted Part A and Part B of the International Ethics Standards Board for Accountants' *Code of Ethics for Professional Accountants* (the IESBA Code) published by the International Federation of Accountants (IFAC) with adaptations, with effect from 1 January 2011. The proposed amendment to the IRBA Code is due to local needs and not as a result of an amendment to the IESBA Code.

The IRBA's Legislative Mandate

The objectives of the Auditing Profession Act, 2005 (Act No.26 of 2005) (the Act) are set out in Section 2 and include, inter alia:

- (c) *"To approve the development and maintenance of internationally comparable ethical standards and auditing standards for auditors that promote investment and as a consequence employment in the Republic; and*
- (d) *To set out measures to advance the implementation of appropriate standards of competence and good ethics in the auditing profession".*

To give effect to the objectives of the Act, Section 4(1) sets out the general functions of the IRBA, including that *"the Regulatory Board must, in addition to its other functions provided for in this Act:*

- (a) *Take steps to promote the integrity of the auditing profession; and*
- (c) *Prescribe standards of professional competence, ethics and conduct of registered auditors".*

Statutory Responsibility of the CFAE

The statutory responsibility of the CFAE is set out in Section 21(2) of the Act and requires that *"the CFAE must assist the IRBA:*

- (a) *To determine what constitutes improper conduct by registered auditors by developing requirements and guidelines for professional ethics, including a code of professional conduct;*
- (b) *To 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*
- (c) *To provide advice to registered auditors on matters of professional ethics and conduct."*

The proposed amendment may be downloaded from the IRBA's website at www.irba.co.za.

Comments should be submitted by **30 June 2016** electronically in Word format to the Director Standards, Imran Vanker, at standards@irba.co.za, or by post to:

REQUEST FOR COMMENTS

The Director Standards

The Independent Regulatory Board for Auditors

PO Box 8237

Greenstone, 1616

South Africa

All comments will be considered a matter of public record and will be posted on the IRBA's website Responses received will assist the CFAE to identify any further needed changes to the proposed amendment.

Should you have any queries, or experience any technical difficulties in downloading the document, please e-mail the Standards Department at standards@irba.co.za or contact:

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The proposed amendment to this Code is based on the local requirements of Part B of the IRBA Code of Professional Conduct for Registered Auditors. The IRBA Code of Professional Conduct adopted the International Ethics Standards Board for Accountants (IESBA) *Code of Ethics for Professional Accountants* published by the International Federation of Accountants (IFAC) and is used with permission of IFAC. Adaptations to Parts A and B are *underlined and in italics*.

EXPLANATORY MEMORANDUM

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EXPLANATORY MEMORANDUM

Introduction

This memorandum provides background to and an explanation of the proposed amendment to the Independent Regulatory Board for Auditors' (IRBA) *Code of Professional Conduct for Registered Auditors* (the IRBA Code). In November 2015 the Committee for Auditor Ethics (CFAE) approved the proposed amendment for issue for public comment for a period of 30 days.

The International Federation of Accountants' (IFAC) copyright permissions' policy permits modifications to the International Ethics Standards Board for Accountants' *Code of Ethics for Professional Accountants* (the IESBA Code) to accommodate jurisdictional requirements in different countries. Consequently, this local amendment is being proposed.

The IRBA welcomes comments on the proposed change. In addition to general comments, it welcomes comments on the specific question that is contained at the end of this memorandum.

Paragraph references refer to the IRBA Code as set out in the 2015 IRBA Manual of Information.

Background

The IRBA mission is as follows: "To endeavour to protect the financial interest of the South African public and international investors in South Africa through the effective and appropriate regulation of assurance conducted by registered assurance providers in accordance with internationally recognised standards and processes."

The IRBA adopted Parts A and B and the Definitions of the International Ethics Standards Board for Accountants' (IESBA) *Code of Ethics for Professional Accountants* (July 2009) published by the IFAC with effect from 1 January 2011. The CFAE comments on all proposed amendments to the IESBA Code and considers final amendments to the IESBA Code for the possible amendment of the IRBA Code. Local adaptations of the IESBA Code are reflected in the IRBA Code and they are underlined and in italics.

Significant Matters

When the IRBA Code was first introduced in January 2011, it included local amendments to Section 270 – Custody of Clients Assets. At the time, the IRBA already had, in issue, a circular¹ to registered auditors dealing with trust monies. The circular was subsequently amplified in the 2011 IRBA Manual of Information to include Section 270. The proposed amendment seeks to clarify the registered auditor's position in respect of holding funds on behalf of a client and seeks to prevent any confusion in this regard.

The extant Section 270.4(a)(ii) requires a client's funds to be placed in "appropriately designated accounts". However, the guidance included in this section suggests that a client's funds may be kept in a general account in the registered auditor's name. This guidance is now considered inappropriate, and in certain circumstances may not be desirable at all. The

¹ Page 7-11 of the 2015 Manual of Information.

use of a general account for holding a client's funds should be avoided since the registered auditor may effectively be placing their client's funds at risk. The risk, for example, could include any of the following:

- (a) Where a registered auditor passes away and the client's funds become part of the deceased estate; or
- (b) In the event of the registered auditor's insolvency, the funds may fall into the insolvent estate at the expense of the true owner and also at the expense of the image of the profession as a whole; or
- (c) In the event of the registered auditor absconding with the fund, the owner of the fund is left with nothing but a personal action against the registered auditor (who might or might not himself carry fidelity insurance).

Once the proposed amendment to Section 270.4 has been adopted, the IRBA's Trust Monies Circular, B.1/1997, will be withdrawn.

The South African Institute of Chartered Accountants (SAICA) has adopted verbatim the local amendments made to the IRBA Code of Professional Conduct in the SAICA Code of Professional Conduct. Thus, the proposed amendment could result in SAICA considering a similar change to its Code of Professional Conduct.

Project Timetable

Subject to comments received during this period, the CFAE plans to finalise the amendment in the last quarter of 2016 before recommending it for approval by the IRBA Board for issue. It is anticipated that the amendment to Section 270.4 in the IRBA Code of Professional Conduct will be effective from **1 March 2017**.

Guide for Respondents

The CFAE welcomes comments on matters addressed in the exposure draft. Comments are most helpful when they refer to specific wording, include the reasons for the comments and, where appropriate, make specific suggestions for any proposed changes to the wording.

Request for Specific Comments

The IRBA welcomes views on the following specific question:

Do you agree with the proposed amendment to Section 270.4? "Yes/No".

If "No", please indicate what additional guidance is needed.

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**PROPOSED CHANGE TO THE CODE OF CONDUCT FOR REGISTERED AUDITORS
ADDRESSING CUSTODY OF CLIENT ASSETS**

The proposed modification appears in Section 270.4(a) and 270.4(b)(ii) below:

S270 Custody of Assets

270.1 A registered auditor shall not assume custody of client monies or other assets unless permitted to do so by law and, if so, in compliance with any additional legal duties imposed on a registered auditor holding such assets.

270.2 The holding of client assets creates threats to compliance with the fundamental principles. For example, there is a self-interest threat to professional behaviour and may be a self-interest threat to objectivity arising from holding client assets. A registered auditor entrusted with money (or other assets) belonging to others shall therefore:

- (a) Keep such assets separately from personal or firm assets;
- (b) Use such assets only for the purpose for which they are intended;
- (c) At all times be ready to account for those assets and any income, dividends, or gains generated, to any persons entitled to such accounting; and
- (d) Comply with all relevant laws and regulations relevant to the holding of and accounting for such assets.

270.3 As part of client and engagement acceptance procedures for services that may involve the holding of client assets, a registered auditor shall make appropriate inquiries about the source of such assets and consider legal and regulatory obligations. For example, if the registered auditor has reason to believe that the assets were derived from illegal activities, such as money laundering, a threat to compliance with the fundamental principles would be created. In such situations, the registered auditor shall not accept or hold the client monies and may consider seeking legal advice, inter alia, with regard to regulatory reporting responsibilities.

270.4 When a registered auditor in the course of providing professional services is entrusted with client monies, or property other than monies belonging to others, the registered auditor shall –

(a) Not refer to funds or property as being held “in trust” or in a “trust accounts”. The term “trust account” is misleading. Clients and members of the public may assume that the term “trust account” connotes a statutory trust account² that is underpinned by statutory fidelity funds which is incorrect.

(b) for all clients monies which come into the registered auditor’s possession or under the registered auditor’s control, and for which the registered auditor is liable to account to a client or any other person:

(i) maintain one or more bank accounts with an institution or institutions registered in terms of the Banks Act, 1990 (Act 94 of 1990) that are separate from the registered auditor’s own bank account; and

² such as those utilised by estate agents and attorneys, and regulated in terms of the Estate Agents and Attorneys Acts

(ii) appropriately designate **(name)** such **bank** accounts (which account or accounts may be a general account in the registered auditor's name or must be in specific accounts operated in the names of the relevant clients or any other person to whom the registered auditor is accountable); and

(iii) deposit client monies without delay to the credit of such client account indicated in **(ab) (i)** and **(ab) (ii)** above; and

(c) for property other than money which comes into the registered auditor's possession or under the registered auditor's control and for which the registered auditor is liable to account to a client or to any other person (including, but without limitation, trust property which is expressly registered in the name of the registered auditor, or jointly in the name of the registered auditor and any other person, in their capacity as administrator, trustee, curator or agent, as the case may be), the registered auditor shall –

(i) maintain such records as may be reasonably expected to ensure that the property can readily be identified as being the property of such client or other person; and

(ii) if the property is in the form of documents of title to money, or documents of title that can be converted into money, shall make such arrangements as may be appropriate in the circumstances to safeguard such documents against unauthorised use.