

Revised Guide
May 2015



Revised Guide for Registered Auditors

**Reportable Irregularities in terms of the Auditing
Profession Act**

Independent Regulatory Board for Auditors
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The purpose of this Revised Guide for Registered Auditors: *Reportable Irregularities in Terms of the Auditing Profession Act* (the Guide) is to provide guidance to registered auditors on their responsibility to report reportable irregularities in terms of section 45 of the Auditing Profession Act, 2005 (Act 26 of 2005) (the APA). Depending on the circumstances, registered auditors are advised to obtain legal advice and are reminded of the responsibility to adequately and appropriately document their deliberations. In this Guide reference to an “auditor” or a “registered auditor”, unless the context requires otherwise, means an auditor registered as such under the APA.

This Guide does not apply to a registered auditor acting as an independent reviewer in terms of section 30(2)(b)(ii)(bb) of the Companies Act, 2008 (Act No. 71 of 2008) (the Companies Act), who identifies a reportable irregularity in terms of Regulation 29 to the Companies Act, which must be reported directly to the Companies and Intellectual Property Commission (CIPC). Note that the definition of reportable irregularity under Regulation 29 differs from that set out in the APA.

This Guide replaces the Guide *Reportable Irregularities: A Guide for Registered Auditors* issued in June 2006, which has been withdrawn.

When using this Guide auditors should bear in mind that there might have been amendments to the IRBA Code of Professional Conduct, Laws or Regulations made subsequent to the issue date of this Guide.

This Guide is divided into four parts:

Part 1: Provides the definition of a reportable irregularity and general principles.

Part 2: Deals with when the obligation to report irregularities arises and highlights when this Guide becomes applicable. It also highlights the process followed by the Independent Regulatory Board for Auditors (IRBA) on receipt of a reportable irregularity report made in terms of section 45.

Part 3: Deals with the impact of a section 45 reportable irregularity on the auditor’s report.

Part 4: Deals with professional responsibilities, disciplinary measures, other sanctions and monitoring of compliance with section 45.

This Guide for Registered Auditors: *Reportable Irregularities in terms of the Auditing Profession Act (Revised)* may be downloaded free-of-charge from the IRBA website: www.irba.co.za.

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**REVISED GUIDE FOR REGISTERED AUDITORS:
REPORTABLE IRREGULARITIES IN TERMS OF THE AUDITING PROFESSION ACT**

(Effective from 1 July 2015)

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This Revised Guide for Registered Auditors: *Reportable Irregularities in Terms of the Auditing Profession Act* provides guidance to registered auditors (auditors) in implementing the requirements of the Auditing Profession Act, 2005 (Act 26 of 2005) (the APA) when reporting reportable irregularities, in terms of section 45.

Guides are developed and issued by the IRBA to provide guidance to auditors in meeting specific legislative requirements imposed by a Regulator. Guides do not impose requirements on auditors beyond those included in the International or South African Standard/s or South African regulatory requirements and do not change an auditor's responsibility to comply, in all material respects, with the requirements of the International or South African Standards or with South African regulatory requirements relevant to the audit, review, other assurance services or related services engagement.

An auditor is required to have an understanding of the entire text of every Guide to enable the auditor to assess whether or not any particular Guide is relevant to an engagement, and if so, to enable the auditor to apply the requirements of the particular International or South African Standard/s to which the Guide relates, properly.

In terms of section 1 of the APA, a Guide is included in the definition of "auditing pronouncements" and in terms of the APA, the auditor must, in the performance of an audit, comply with those standards, practice statements, guidelines and circulars developed, adopted, issued or prescribed by the Regulatory Board.

Part 1 - Definition and general principles

1 Section 1 of the APA

- 1.1 Section 1 of the APA defines a reportable irregularity as follows:
“reportable irregularity” means any unlawful act or omission committed by any person responsible for the management of an entity, which —
- (a) *has caused or is likely to cause material financial loss to the entity or to any partner, member, shareholder, creditor or investor of the entity in respect of his, her or its dealings with that entity; or*
 - (b) *is fraudulent or amounts to theft; or*
 - (c) *represents a material breach of any fiduciary duty owed by such person to the entity or any partner, member, shareholder, creditor or investor of the entity under any law applying to the entity or the conduct or management thereof.*

2 An unlawful act or omission

- 2.1 For a reportable irregularity to exist there must be an unlawful act or omission, committed by any person responsible for the management of an entity.
- 2.2 An unlawful act or omission would be an act or omission which is contrary to any law passed by a government which applies to the activities of the entity, an act or omission which is contrary to regulation, or an act or omission which is contrary to accepted common law principles.
- 2.3 Such an unlawful act or omission might arise as a result of negligence or due to the intentional act or omission of any person responsible for management of the entity (discussed in section 3). Unlawful acts or omissions include the negligent or intentional breach of laws in the various jurisdictions in which the entity operates.
- 2.4 The registered auditor (the auditor)¹ responsible for the engagement (see 6.1), considers reporting a reportable irregularity only if the auditor is satisfied or has reason to believe that the unlawful act or omission is committed by a person responsible for the management of the entity.

¹ Section 44(1)(a) of the APA requires that, where the registered auditor is a firm, the firm must immediately take a decision as to the individual registered auditor or registered auditors within the firm that is responsible and accountable for that audit

- 2.5 An auditor is not a legal expert and performs an audit in accordance with the auditing pronouncements issued by the IRBA. The APA does not introduce additional audit procedures required to be performed for the purposes of detecting reportable irregularities.
- 2.6 In the audit of financial statements the auditor is required, amongst others, to comply with International Standard on Auditing (ISA) 250, *Consideration of Laws and Regulations in an Audit of Financial Statements*. The auditor's responsibility to consider compliance with laws and regulations is intrinsically linked to the auditor's overall objective of expressing an opinion on the financial statements. Ordinarily, the further removed non-compliance is from the events and transactions reflected in the financial statements, the less likely the auditor is to become aware of it or to recognise the non-compliance. ISA 250 requires that the auditor obtain sufficient appropriate audit evidence regarding compliance with the provisions of those laws and regulations generally recognised to have a direct effect on the determination of material amounts and disclosures in the financial statements. Furthermore, the auditor is required to perform specified audit procedures to help identify instances of non-compliance with other laws and regulations that may have a material effect on the financial statements. ISA 250 (paragraph 4) states that the requirements are designed to assist the auditor in identifying material misstatement of the financial statements due to non-compliance with laws and regulations, but that the auditor is not responsible for preventing non-compliance and cannot be expected to detect non-compliance with all laws and regulations.
- 2.7 The auditor's training, experience and understanding of the entity and its industry should provide a basis for recognition that some acts or omissions coming to the auditor's attention may constitute non-compliance with laws and regulations.
- 2.8 The determination as to whether a particular act or omission constitutes or is likely to constitute non-compliance can ultimately only be made by a court of law. The auditor therefore only has the duty to report the unlawful act or omission as a reportable irregularity where, based on the professional judgement of the auditor, he/she has evidence that, on the face of it, causes the auditor to be satisfied or have reason to believe that the unlawful act or omission meets the definition of a reportable irregularity. Depending on the circumstance, in cases of uncertainty or complexity the

auditor is advised to obtain legal advice. Ultimately it is the auditor's decision as to whether the auditor reasonably believes that a reportable irregularity exists; there should not be blind reliance on a legal opinion or the abrogation of the auditor's responsibility. The auditor then reports the reportable irregularity in good faith, based on the information that has come to the auditor's attention. 'Satisfied' in the context of this section does not mean that the auditor has to be satisfied that the person involved will be found to have contravened any law. It is also important to note that the *auditor* only needs to have *reason to believe* and not necessarily *to be satisfied* that an unlawful act or omission had occurred. (Discussed in Appendix 6).

Cross border audits

- 2.9 A circumstance may arise where a foreign subsidiary or component of a South African company contravenes a law or regulation, either South African or foreign. Such an unlawful act or omission would constitute a reportable irregularity where the management of the South African company were involved, or knew or reasonably should have known, about the illegal act or omission, and failed to act appropriately.

3 Committed by any person responsible for management of an entity

- 3.1 For a reportable irregularity to exist there must be an unlawful act or omission on the part of a person responsible for management of an entity. In establishing whether the person is responsible for management, the auditor should consider the following:
- 3.1.1. The definition of management in the Handbook of International Quality Control, Auditing, Review, Other Assurance and Related Services Pronouncements, is "*the person(s) with executive responsibility for the conduct of the entity's operations. For some entities in some jurisdictions, management includes some or all of those charged with governance, for example, executive members of a governance board, or an owner-manager*".
- 3.1.2. The APA defines the management board as: "*in relation to an entity which is a company, means the board of directors of the company and, in relation to any other entity, means the body or individual responsible for the management of the business of the entity*".

- 3.1.3. The provisions of the Companies Act of South Africa No. 71 of 2008 (Act No. 71 of 2008) (the Companies Act) and the Regulations thereto:
- 3.1.3.1 Prescribe that the business and affairs of a company must be managed by or under the direction of its board, which has the authority to exercise all the powers and perform any of the functions of the company, except to the extent that the Companies Act or the company's Memorandum of Incorporation provides otherwise. (Section 66(1))
- 3.1.3.2 Establish the designation of a prescribed officer being a person who:
“exercises general executive control over and management of the whole, or a significant portion, of the business and activities of the company; or regularly participates to a material degree in the exercise of general executive control over and management of the whole, or a significant portion, of the business and activities of the company”. (Regulation 38)
- 3.1.3.3 Impose on directors and prescribed officers and persons who are members of a committee of a board of a company, or of the audit committee of the company, the same standards of conduct and liability as set out in the Companies Act and in accordance with the principles of the common law. (Sections 76, 77)
- 3.1.4 When an auditor considers whether a person is responsible for management of an entity, the auditor determines whether the person is responsible for or regularly participates to a material degree in the executive control over and management of the whole, or a significant portion of the business i.e. the decision-making and policymaking as well as the supervision and administration of the business. Lesser levels of management (i.e. those who are **not** considered to exercise general executive control over and management of the whole or a significant portion of the business and activities of the company) would be those who are expected to implement the policies and decisions of executive management. While other levels of management may make decisions and set policies, these are specific to their functions and areas of responsibility and do not extend to the organisation as a whole. Examples of executive management's responsibilities could include:
- Setting the strategic objectives and operational policies of the entity;

- Allocating resources within the entity to achieve the strategic objectives and support the operational policies of the entity; or
- Selecting accounting policies, reviewing and authorising the financial statements, and authorising the personnel to act within predefined guidelines and frameworks.

3.1.5 The auditor should consider whether the individual is responsible for the management of the entity, regardless of his/her title and position. Individuals who are not employees of the company are not precluded from being responsible for the management of the entity. There may be situations where the individual is part of the management of the holding company, is a contractor or outsourced service provider exercising managerial decisions, or is a business rescue practitioner.

3.1.6 An unlawful act or omission of an employee of an entity with the knowledge of or under the direction of a person responsible for management would, in the context of the above, be viewed by the auditor as an unlawful act or omission by a person responsible for the management of the entity.

4 Circumstances under which an unlawful act or omission is reportable²

4.1 Unlawful acts or omissions which are reportable are set out in sections (a) to (c) of the definition of a “**reportable irregularity**”. Each circumstance would give rise to a reportable irregularity and accordingly guidance is provided in respect of each circumstance.

An unlawful act or omission is one which:

- (a) *has caused or is likely to cause material financial loss to the entity or to any partner, member, shareholder, creditor or investor of the entity in respect of his, her or its dealings with that entity; or*
- (b) *is fraudulent or amounts to theft; or*
- (c) *represents a material breach of any fiduciary duty owed by such person to the entity or any partner, member, shareholder, creditor or investor of the entity under any law applying to the entity or the conduct or management thereof.*

² Refer to Appendix 1 for a diagrammatic presentation to determine whether an irregularity is reportable

Note that each circumstance represents an independent basis for a report. In many instances the unlawful act or omission may meet the requirements of more than one of the defined criteria in which event the auditor will set out each of the applicable circumstances in the report.

4.2 *Material financial loss*

(a) <i>“has caused or is likely to cause material financial loss to the entity or to any partner, member, shareholder, creditor or investor of the entity in respect of his, her or its dealings with that entity”</i>
--

4.2.1 If the unlawful act or omission by any person responsible for the management of the entity has the consequence of causing or being likely to cause material financial loss to any of the parties named then the act or omission is reportable. Both quantitative and qualitative factors could be relevant in making such a determination.

4.2.2 In the quantitative sense the measure of materiality should be applied within the context of the absolute financial loss caused by the unlawful act or omission and not the level of materiality as applied for purposes of the audit of the financial statements (or any audit of financial or other information).

4.2.3 While it is difficult to set a materiality level, the auditor considers the relative size of the loss or potential loss and its nature and circumstances of occurrence with regard to such parties on the basis of the auditor’s professional judgment having regard to the nature and value of their individual or collective dealings with the entity.

4.2.4 The auditor may not take into account any benefit that may arise from a reportable irregularity committed by management, for example, any benefit arising from the payment of a bribe. It would be inappropriate for an auditor to justify a decision not to report on the basis of a net position resulting from an irregularity.

Dealings with that entity

4.2.5 An unlawful act or omission by a person responsible for the management of the entity which has directly caused or is likely to cause material financial loss to any partner, member, shareholder, creditor or investor of the entity in respect of his, her or its particular dealings with that entity, and

irrespective of whether it has caused or is likely to cause material financial loss to the entity, is a reportable irregularity.

4.3 *Fraudulent or amounts to theft*

(b) <i>“is fraudulent or amounts to theft”</i>
--

4.3.1 An unlawful act or omission may itself not give rise to material financial loss or potential financial loss, but nonetheless constitutes fraud or amounts to theft. The auditor exercises professional judgment to determine whether an unlawful act or omission constitutes fraud or theft. In cases of uncertainty the auditor should consider obtaining professional or legal advice.

4.3.2 Fraud in this context should be considered in the context of the legal definition of fraud. Fraud has been defined as follows: Fraud is the unlawful and intentional making of a misrepresentation which causes actual prejudice or which is potentially prejudicial to another³. Fraud involves a deliberate deceit, or action, or omission in order to mislead another party to the other party's prejudice. Likewise, theft should also be considered in the context of the legal definition of theft. Theft has been defined as the unlawful and intentional appropriation by a person of another's property⁴.

4.3.3 While fraud can be difficult to determine from a legal perspective, the auditor takes account of the evidence available and draws a conclusion on the possibility that the act or omission of any person responsible for management of the entity may amount to deceit or misrepresentation intended to cause prejudice to another.

4.3.4 ISA 240, *The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements* deals with the auditor's responsibilities relating to fraud in an audit of financial statements. Specifically, it expands on how ISA 315 (Revised), *Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment* and ISA 330, *The Auditor's Responses to Assessed Risks* are to be applied in relation to risks of material misstatement due to fraud. ISA 240 in particular sets out requirements in respect of communication of identified or

³ The Law of South Africa 2nd Edition Volume 6

⁴ State v Visagie 1991(1) SA177(AD).

suspected fraud to Regulatory and Enforcement Authorities (paragraph 43).

4.4 *Material breach of any fiduciary duty*

(c) *“represents a material breach of any fiduciary duty owed by such person to the entity or any partner, member, shareholder, creditor or investor of the entity under any law applying to the entity or the conduct or management thereof”*

4.4.1 A fiduciary duty can be defined as the legal duty of a fiduciary to act in good faith in promoting and protecting the interests of a beneficiary and to avoid a conflict of interest between the fiduciary and the beneficiary.

4.4.2 A person generally comes into a fiduciary relationship when he or she controls the assets of another or holds the power to act in the interest of another. Fiduciaries have a duty to act in good faith on behalf of and for the sole benefit of the person to whom they owe a fiduciary duty, should not put their personal interests before those of the beneficiary and should not profit from their position as a fiduciary. A fiduciary relationship is generally marked by three characteristics:

- there is scope for the exercise of some discretion or power;
- that power or discretion can be used unilaterally so as to affect the beneficiary's legal or practical interests;
- the beneficiary is vulnerable to the exercise of that discretion or power.

4.4.3 In the context of a company, the directors' fiduciary duty^{5/6} is owed to the company and to no one else. The fundamental fiduciary duties owed by directors toward their company under the common law include:

- preventing a conflict of interest;
- not exceeding the limitations of their power;
- maintaining an unfettered discretion;
- exercising their powers for the purpose for which they were conferred;

⁵ See *Phillips v Fieldstone Africa (Pty) Ltd* 2004(3); SA 465 (SCA) for a review of the law relating to the fiduciary duties of directors)

⁶ Refer also to section 76 of the Companies Act

- not exercising their powers for an improper or collateral purpose;
- dealing with the company openly and in good faith;
- not making a secret profit;
- not taking certain economic opportunities for themselves;
- not competing with the company; and
- not misusing confidential information.

4.4.4 Examples of fiduciary relationships include, without being exhaustive:

- A director or prescribed officer in respect of his or her relationship to a company;
- A member in respect of his or her relationship to a close corporation;
- A partner in respect of his or her relationship to his or her co-partners; and
- A trustee in his or her relationship to the beneficiaries of the trust.

Whether or not a fiduciary relationship exists will depend on the facts of the particular case⁷.

4.4.5 Materiality is viewed in the context of the nature of the breach and not purely in financial terms. The auditor determines the nature of the fiduciary duty and assesses the materiality of the breach having regard to its impact and consequences. The purpose for which the fiduciary duty was established, the impact upon governance within the entity and the consequences for the entity and third parties ought to be considered as well as the important requirement of loyalty and good faith expected of those responsible for management.

4.4.6 The auditor should consider all relevant factors when assessing whether a breach of fiduciary duty is material, including:

- History of non-compliance - is the non-compliance a recurring/on-going feature?

⁷ Volvo (Southern Africa) (Pty) Ltd vs Yssel 2009(6) SA 531 (SCA)

- Responsiveness of management to compliance. Wilful disregard for compliance, even for a seemingly trivial issue, should be seen in a serious light.
- Number of areas of non-compliance (evaluation of materiality of items in aggregate as well as individually). Multiple seemingly trivial instances of non-compliance should be carefully considered as they may collectively indicate a material breach of fiduciary duty.

The mere failure to comply with statutory requirements does not by itself amount to a breach of fiduciary duty in every instance. The auditor may consider obtaining legal advice in cases of uncertainty.

Part 2 – When the obligation to report reportable irregularities arises and the process of dealing with reportable irregularities in terms of section 45

5 Requirements of section 45⁸

5.1 The requirements are set out in section 45 of the APA:

- (1)(a) *An individual registered auditor referred to in section 44(1)(a)⁹ of an entity that is satisfied or has reason to believe that a reportable irregularity has taken place or is taking place in respect of that entity must, without delay, send a written report to the Regulatory Board.*
- (b) *The report must give particulars of the reportable irregularity referred to in subsection (1)(a) and must include such other information and particulars as the registered auditor considers appropriate.*
- (2)(a) *The registered auditor must within three days of sending the report to the Regulatory Board notify the members of the management board of the entity in writing of the sending of the report referred to in subsection (1) and the provisions of this section.*
- (b) *A copy of the report to the Regulatory Board must accompany the notice.*
- (3) *The registered auditor must as soon as reasonably possible but no later than 30 days from the date on which the report referred to in subsection (1) was sent to the Regulatory Board —*
 - (a) *take all reasonable measures to discuss the report referred to in subsection (1) with the members of the management board of the entity;*

⁸ Refer to Appendix 2 for a diagrammatic presentation of the process to deal with a reportable irregularity

⁹ *Section 44(1)(a) provides: Where a registered auditor that is a firm is appointed by an entity to perform an audit, that firm must immediately after the appointment is made, take a decision as to the individual registered auditor or registered auditors within the firm that is responsible and accountable for that audit*

provisional trustee or trustee, or a provisional liquidator or liquidator, as the case may be, at the same time as the report is sent to the Regulatory Board or as soon as reasonably possible after his or her appointment; or

(b) has not sent a report referred to in subsection (1) or (3), and is requested by a provisional trustee or trustee, or a provisional liquidator or liquidator, as the case may be, to send a report, the registered auditor must as soon as reasonably possible –

(i) send the report together with a motivation as to why a report was not sent; or

(ii) submit a notice that in the registered auditor's opinion no report needed to be submitted, together with a justification of the opinion.

6 When the obligation to report a reportable irregularity arises and the responsibility to report

6.1 *Section 45(1) provides as follows:*

(a) An individual registered auditor referred to in section 44(1)(a) of an entity that is satisfied or has reason to believe that a reportable irregularity has taken place or is taking place in respect of that entity must, without delay, send a written report to the Regulatory Board.

6.1.1 The auditor or, in the case of companies or partnerships, the individual auditor/s identified by the audit firm to take responsibility and accountability for the audit, has the sole responsibility to report a reportable irregularity to the IRBA.

6.1.2 The obligation to report arises when:

- an auditor is appointed by an entity to perform an audit which is defined in section 1 of the APA as:

“audit” means the examination of, in accordance with prescribed or applicable auditing standards –

(a) financial statements with the objective of expressing an opinion as to their fairness or compliance with an identified financial

reporting framework and any applicable statutory requirements;
or

(b) financial and other information, prepared in accordance with suitable criteria, with the objective of expressing an opinion on the financial and other information.

- the auditor is satisfied or has reason to believe that an unlawful act or omission committed by any person responsible for the management of that entity, and which meets the requirements of the definition of a reportable irregularity, has taken place or is taking place in respect of that entity, based on the information which comes to the knowledge of the auditor from any source.

6.1.3 Section 45(1)(a) imposes a statutory duty to report a reportable irregularity on the individual auditor (or on the auditors identified by the 'audit firm') who is responsible and accountable for the engagement (section 44(1)(a)).

6.1.4 Paragraph (a) of the definition of "audit" relates to an audit of financial statements, and as such any engagement to express an opinion as to fairness or compliance with an identified financial reporting framework and any applicable statutory requirements will result in the client of the audit firm being an audit client.

6.1.5 Paragraph (b) of the definition of "audit" addresses any other examination of financial and other information, prepared in accordance with suitable criteria, with the objective of expressing an opinion on such financial and other information. The audit of other information includes other reasonable assurance engagements as provided for in International and South African auditing pronouncements. It excludes limited assurance engagements and independent reviews of financial statements performed under International Standard on Review Engagements (ISRE) 2400 (Revised), *Engagements to Review Historical Financial Statements*. However, review engagements performed under ISRE 2410, *Review of interim Financial Information Performed by the Independent Auditor of the Entity*, are included since in these circumstances the auditor is appointed to audit the annual financial statements.

6.1.6 If the audit firm provides services other than the audit of financial and other information (for example performing an agreed-upon procedures engagement) but the client is nevertheless an audit client of the audit firm,

the auditor considers any information which comes to the knowledge of the auditor while performing those professional services which may cause the auditor to be satisfied or have reason to believe that a reportable irregularity has taken place or is taking place. Another example would be where the audit firm, in conducting a forensic investigation at a client that is also an audit client of the firm is satisfied or has reason believe that a situation exists, which meets the conditions of being reportable. Where such a situation exists, such information should be brought to the attention of the individual auditor by the person responsible for providing the other professional service.

- 6.1.7 Once the auditor is satisfied or has such reason to believe¹⁰ that a reportable irregularity has taken place or is taking place, the auditor, **“without delay”**¹¹, issues a written report to the IRBA (‘the first report’)¹².
- 6.1.8 The auditor should retain documentation to support the auditor’s conclusion in determining whether or not an unlawful act or omission meets the definition of a reportable irregularity.
- 6.1.9 Audits performed on behalf of the Auditor-General (AG) do not result in a responsibility for the auditor to report the reportable irregularity to the IRBA. The auditor in this instance should report the matter to the AG, because the entity has not appointed the auditor. However, in circumstances where the AG has opted not to audit the entity, and such public sector entity appoints the auditor, the auditor reports the reportable irregularity to the IRBA.
- 6.1.10 The auditor also considers whether or not he or she should in addition report the act or omission in accordance with any other legislation, for example the Financial Intelligence Centre Act, No. 38 of 2001, as amended (FICA) or The Prevention and Combating of Corrupt Activities Act No. 12 of 2004 (PRECCA).
- 6.2 *Consideration of unlawful acts or omissions where more than one auditor is responsible and accountable for an audit*

¹⁰ Refer to Appendix 6 for guidance with regards to failing to report a reportable irregularity

¹¹ Refer to section 8 for guidance with regards to reporting “without delay”

¹² Refer to Appendix 3 for an illustrative example of an auditor’s first report to the IRBA

6.2.1 If more than one auditor is responsible and accountable for an audit engagement (such as in a joint audit where an auditor is appointed by each audit firm), the duty to consider whether an unlawful act or omission is a reportable irregularity lies with each individual auditor. Depending on whether both auditors or only one of them are satisfied or have reason to believe that a reportable irregularity exists, the auditor's responsibilities are as follows:

- If both individual auditors are satisfied or have reason to believe that the unlawful act or omission meets the definition of a reportable irregularity:
 - The auditors responsible and accountable for the audit may send a combined report in terms of section 45; or
 - Each individual auditor responsible and accountable for the audit may send a separate report, and still comply with the requirements of section 45.
- If only one auditor is satisfied or has reason to believe that the unlawful act or omission meets the definition of a reportable irregularity such auditor must send a report in terms of section 45 to comply with the requirements of the section. A copy of the report should also be sent to the other auditor.

6.3 *Reportable irregularities identified at subsidiary or component level within a group of companies*

6.3.1 In a group audit engagement, the auditor performing the audit of a subsidiary or component will not have a responsibility to report a reportable irregularity if the subsidiary or component is not required to have a statutory audit of the financial statements i.e. the subsidiary or component is only being subject to audit for the purposes of the group opinion on the group financial statements. However, where the auditor performing the audit of a subsidiary or component will issue a separate audit opinion on the financial statements of the subsidiary or component, that auditor has a responsibility to report a reportable irregularity if one is identified in the subsidiary or component.

6.3.2 Where a reportable irregularity has occurred at a subsidiary or component within a group and the auditor's report on the subsidiary's or component's

annual financial statements included an appropriate notification on the basis of section 45, the auditor responsible for the audit of the group financial statements (group auditor) should consider whether the reportable irregularity will affect the group. The group auditor will apply the criteria of the definition of a reportable irregularity to the group as a whole with regard to the reportable irregularity identified in the subsidiary or component - for example, considering whether group management was also involved in the unlawful acts or omissions. Where the group auditor is satisfied that the reportable irregularity applies to the group, the group auditor acts in accordance with section 45. The group individual auditor modifies his or her auditor's report as appropriate on the group where he or she has complied with section 45 (Discussed in Part 3 of the Guide). Where a reportable irregularity occurs and is reported at subsidiary level, the auditor of the subsidiary should provide a copy of the reportable irregularity report to the group auditor.

- 6.3.3 The group auditor and subsidiary auditor may be the same person. In such circumstances it may be appropriate, particularly in terms of timing, to apply the considerations of section 45 to the subsidiary and the group simultaneously.

7 Identification of a possible reportable irregularity

- 7.1 Section 45(5) of the APA states:

For the purpose of the reports referred to in subsections (1) and (3), a registered auditor may carry out such investigations as the registered auditor may consider necessary and, in performing any duty referred to in the preceding provisions of this section the registered auditor must have regard to all the information which comes to the knowledge of the registered auditor from any source.

- 7.1.1 In considering a matter relating to a potential reportable irregularity the auditor, or the firm, as the case may be, considers all information which comes to the knowledge of the auditor or the knowledge of the firm from any source.

- 7.1.2 This will require the auditor to consider information gained when providing services of another nature to the audit client, or providing services to another client which provides information in relation to an audit client and which would otherwise have been ignored due to the confidentiality

requirements contained in the *IRBA Code of Professional Conduct for Registered Auditors* (the IRBA Code).

- 7.1.3 The auditor also considers matters which come to the auditor's knowledge from third party sources. For instance, criminal charges, allegations of non-compliance raised, press coverage of suspicions, or inquiries directed to the auditor would be information which the auditor should consider in determining whether a reportable irregularity exists.
- 7.1.4 The auditor can reasonably be expected to consider the reliability of the source, the nature of the information and the relationship of such information to other knowledge regarding the entity. Based on such considerations the auditor decides whether to investigate the information further at that stage.
- 7.1.5 In terms of section 45(5), the auditor only has to consider information which comes to the auditor's attention. There is no requirement or onus on the auditor in terms of the APA to design procedures and inquiries to discover reportable irregularities. The requirement is solely for the auditor to respond to any information that comes to the attention of the auditor. The requirement of section 45(5) does not detract from the auditor's responsibilities in terms of ISA 240.
- 7.1.6 An auditor may carry out such investigations as the auditor may consider necessary to enable the auditor to report in terms of the APA.
- 7.1.7 The investigations are designed only to provide the auditor with sufficient grounds to be satisfied or have reason to believe that a reportable irregularity has taken place or is taking place. Although investigations may or may not include discussions with management, such investigations are not designed to provide management with time to rectify the situation so as to avoid the auditor issuing the first report on the potential reportable irregularity.

8 Reporting 'without delay'

- 8.1 The reference to 'without delay' in section 45(1) should be interpreted as applying from the time when the auditor is satisfied or has reason to believe that a reportable irregularity exists, based on the information which has come to the auditor's attention. A delay in breach of the section would occur, for example, whenever an auditor who is so satisfied or has such

reason to believe defers reporting solely because the auditor is waiting on management to rectify the circumstances. The 'reasonable auditor' test is appropriate in these circumstances, i.e., the time a reasonable auditor would take to report the irregularity once he or she is satisfied or has reason to believe that the reportable irregularity has taken or is taking place. Other circumstances may also arise where delay may occur, but this may not necessarily result in the auditor not complying with the provisions of this section, for example, obtaining legal advice in determining whether an act or omission is a reportable irregularity as defined. However the period for obtaining legal advice should not be unreasonably long, as the suspected reportable irregularity may be continuing to the detriment of the relevant affected parties.

9 Informing clients on the auditor's responsibility in terms of section 45

- 9.1 To ensure that the client understands the auditor's responsibility in terms of section 45, it is recommended that engagement letters, whether it be for 'audit' engagements as defined or for other professional services provided, include suitable wording which indicates this responsibility as well as the legal requirements imposed on the auditor by the APA.

10 Reasonable measures to discuss the report with members of the management board of the entity¹³

- 10.1 The paragraphs below are included to provide clarity on what the auditor should consider in complying with the provisions in the APA which require that reasonable measures should be taken to discuss the report in section 45(1) with the members of the management board of the entity, as contemplated by section 45(3)(a).
- 10.2 The requirement of reasonableness involves the application of an objective test based upon the measures which ought to be taken by a 'reasonable auditor'.
- 10.3 The concept of a discussion involves an interactive process between the auditor and the management board. The auditor has no means of compelling the management board to enter into that interactive process with him or her. Section 45(2)(a) requires the auditor to send a copy of the irregularity report to the members of the management board within three

¹³ Refer to Appendix 4 for an illustrative example of an auditor's letter to the management board of the entity

days of sending the report to the IRBA. Section 45(3)(a) then requires the auditor to take reasonable measures to discuss the report with “*the members of the management board of the entity*”. The auditor is required to afford “*the members of the management board of the entity an opportunity to make representations in respect of the report*” (section 45(3)(b)). It is relevant to note that the requirement of reasonableness is only specified in relation to the attempts to discuss the report with the management board. This is because the legislature recognises that the auditor has no mechanism to compel the board to interact with him or her.

10.4 The other consideration is that the section contemplates that the discussions and representations will be with or by “*the members of the management board*” collectively. Each individual case should be judged according to the prevailing facts. An auditor dealing with a properly constituted and active management board would not act in the same way as an auditor dealing with a management board which has abandoned its responsibilities or a management board that is active but unable to execute its responsibilities in the short term due to unforeseen circumstances.

10.5 What can be expected of the auditor can be summarised as follows:

10.5.1 “*reasonable measures*” would include at least the following conduct depending upon the circumstances of the case:

- Extending an invitation to discuss the matter to the board by clear and appropriate communication at the earliest reasonable opportunity.
- The invitation be recorded in writing and it might be most conveniently done by incorporating the invitation to discuss the matter in the notice addressed to the management board under section 45(2)(a).
- If the auditor has reasonable grounds for believing that the systems and administration of the entity are such that one collective notice to the management board will be properly disseminated by the entity then one such notice would be appropriate. If, however, there is any reasonable basis for believing that the invitation will not be extended to all members of the management board then the auditor would consider all other reasonable means to address individual invitations to each board member.
- The auditor is not required to assume the role of tracing agent or to publish notices in the mass media.

- The invitation extended should indicate the auditor's reasonable availability both from the perspective of time and venue. The absence of any response from the management board may lead the auditor to take reasonable steps to establish that the notice/invitation has reached its destination.
- The wording of the notice/invitation should clearly reflect that if the management board fails or declines to engage in discussion with the auditor, then the matter will proceed in conformity with the requirements of section 45.

10.5.2 If the auditor has taken all reasonable measures to communicate with the management board of the entity but is unable to do so through no fault of the auditor, then the auditor should submit a statement, together with the second report sent to the IRBA in terms of section 45(3)(c), that the auditor has taken all reasonable measures but has been unable to discuss the report referred to in section 45(1) with the members of the management board of the entity.

10.6 The auditor considers the response of the management board of the entity and within 30 days from the date on which the report referred to in s45(1) was sent to the IRBA, sends a second report¹⁴ to the IRBA which report must include:

- (i) *a statement that the registered auditor is of the opinion that —*
 - (aa) *no reportable irregularity has taken place or is taking place;*
or
 - (bb) *the suspected reportable irregularity is no longer taking place and that adequate steps have been taken for the prevention or recovery of any loss as a result thereof, if relevant; or*
 - (cc) *the reportable irregularity is continuing; and*
- (ii) *detailed particulars and information supporting the statement referred to in subparagraph (i).*

¹⁴ Refer to Appendix 5 for an illustrative example of an auditor's second report to the IRBA

- 10.7 The IRBA cannot grant an extension to the stipulated period of reporting (no later than 30 days as prescribed by section 45(3)) and the auditor must strictly report within the period.
- 10.8 The auditor should be cognisant of any reporting obligation to another body/regulator which may arise from any other legislation in addition to the requirements of section 45.

11 The IRBA's duty to report to any appropriate regulator

- 11.1 An "appropriate regulator" is defined in terms of section 1 of the APA:
"appropriate regulator", in relation to any entity, means any national government department, registrar, regulator, agency, authority, centre, board or similar institution established, appointed, required or tasked in terms of any law to regulate, oversee or ensure compliance with any legislation, regulation or licence, rule, directive, notice or similar instrument issued in terms of or in compliance with any legislation or regulation, as appears to the Regulatory Board to be appropriate in relation to the entity.
- 11.2. The IRBA will as soon as possible after receipt of the second report containing a statement that the reportable irregularity is continuing notify any appropriate regulator/s in writing of the details of the reportable irregularity to which the report relates and provide it with a copy of the report.

12 Access to information pertaining to a Reportable Irregularity

- 12.1 The APA does not in any section prohibit the auditor from providing the second report to the management board of the audit client. Based on a legal opinion obtained by the IRBA, the IRBA is of the view that the **management board** of the audit client is entitled to a copy of the second report (which contains allegations about their unlawful conduct) and can request it, in writing, from the auditor who is not entitled to refuse to provide a copy to the management board. The auditor is obliged to deny access to these reports in terms of section 140 of the IRBA Code and may not disclose the information obtained and giving rise to the first and second reports made under section 45 to shareholders, creditors, investors or third parties of the audit client who are not directors other than by way of an appropriate notification (or both a modified opinion and a notification) in an auditor's report (see Part 3 of this Guide). There may, however, be a professional obligation to provide a copy of the reportable irregularity

reports to the group auditors or joint auditors and access may be allowed in these situations.

- 12.2 Following the reporting by the IRBA to the appropriate regulator in terms of paragraph 11.2 an auditor may receive a request from the relevant regulator to provide information, in such an event the auditor should refer to the *Guide for Registered Auditors: Access to Audit Working Papers* issued by the IRBA, which provides guidance to auditors when requested to provide access, in particular circumstances, to their audit working papers.
- 12.3 Auditors who are unsure about the legal requirements to be met by the other party before granting access to audit working papers or the reportable irregularity letters are advised to seek legal advice.

Part 3 - The impact of reportable irregularities on the auditor's report

13 Requirements of section 44 of the APA

13.1 Section 44 provides as follows:

(2) *The registered auditor may not, without such qualifications as may be appropriate in the circumstances, express an opinion to the effect that any financial statement or any supplementary information attached thereto which relates to the entity —*

(a) *fairly presents in all material respects the financial position of the entity and the results of its operations and cash flow; and*

(b) *are properly prepared in all material aspects in accordance with the basis of the accounting and financial reporting framework as disclosed in the relevant financial statements.*

unless a registered auditor who is conducting the audit of an entity is satisfied about the criteria specified in subsection (3).

(3) *The criteria referred to in subsection (2) are —*

.....

(e) *that the registered auditor has not had occasion, in the course of the audit or otherwise during the period to which the auditing services relate, to send a report to the Regulatory Board under section 45 relating to a reportable irregularity or that, if such a report was so sent, the registered auditor has been able, prior to expressing the opinion referred to in subsection (1), to send to the Regulatory Board a notification under section 45 that the registered auditor has become satisfied that no reportable irregularity has taken place or is taking place;.....*

14 Application of section 44

14.1 In the context of the APA, the reference to “*without such qualifications as may be appropriate in the circumstances*” could result in a modified audit opinion as contemplated by ISA 705, *Modifications to the Opinion in the Independent Auditor's Report*, if fair presentation is affected and a

notification to the reader of the auditor's report in the Report on Other Legal and Regulatory Requirements that the auditor has reported a reportable irregularity in terms of ISA 700, *Forming an Opinion and Reporting on Financial Statements*. When a reportable irregularity does not affect the fair presentation of the financial statements the auditor notifies the reader of the auditor's report in the Report on Other Legal and Regulatory Requirements section that the auditor has reported a reportable irregularity in terms of ISA 700.

14.2 The auditor is unable to issue an auditor's report on financial statements or supplementary information thereto without including an appropriate notification (or both a modified opinion and a notification), in the event that:

- The reporting process to IRBA is incomplete;
- A reportable irregularity did exist, even if it is no longer taking place and in respect of which adequate steps have been taken for the prevention or recovery of any loss as a result thereof, if applicable; or
- A reportable irregularity existed which could not be/was not corrected (i.e. the reportable irregularity is continuing).

14.3 Therefore, the fact that a reportable irregularity which existed is no longer taking place and adequate steps have been taken for the prevention or recovery of any loss as a result thereof, would nonetheless require the inclusion of an appropriate notification (or both modified opinion and a notification) in the auditor's report on financial statements or supplementary information thereto.

14.4 A notification that results from a reportable irregularity is included in the Report on Other Legal or Regulatory Requirements section of the auditor's report (refer to ISA 700 paragraph 38 for guidance).

14.5 An example of such notification may be:

- Where management has made adequate and appropriate disclosure and the financial statements are fairly presented, in all material respects:

“Report on Other Legal and Regulatory Requirements

In accordance with our responsibilities in terms of sections 44(2) and 44(3) of the Auditing Profession Act, we report that we have identified a reportable irregularity in terms of the Auditing Profession Act. We have reported such matter to the Independent Regulatory Board for

Auditors. The matter pertaining to the reportable irregularity has been described in note xx to the financial statements.”

- Where management has not made adequate and appropriate disclosure and the financial statements are fairly presented, in all material respects, the auditor discloses the information relating to the reportable irregularity in the auditor’s report.

Depending on the circumstances, the auditor should consider whether it is appropriate to add explanatory text following the notification paragraph required in terms of section 44, for example:

- “Management have been unable within the period of 30 days allowed by the Auditing Profession Act to satisfy us that such conduct did not amount to a reportable irregularity”; or
- “Management have responded to the circumstances and conduct in question to the extent that we believe no further loss is being experienced and such loss as was experienced has been recovered [or steps to recover such loss have been initiated by management].”; or
- “The conduct which may have been [fraudulent] [amounted to theft] [a breach of a material fiduciary duty owed] and amounted to a reportable irregularity is to the best of our knowledge [no longer occurring] [continues at the date of this report to be evident].”

14.6 The APA does not require the inclusion of “such qualification as may be appropriate in the circumstances” in respect of:

- Other reasonable assurance reports on matters other than financial statements or supplementary information thereto (reasonable assurance engagements in terms of ISAE 3000 (Revised), *Assurance Engagements Other Than Audits or Reviews of Historical Financial Information*);

However, where the auditor or audit firm has also been appointed to perform an audit of the entity’s financial statements, the auditor considers in the circumstances whether such a qualification is appropriate in the context of such other assurance report. The auditor documents this consideration and the conclusion reached.

or

- A review report on interim financial statements (in terms of ISRE 2410).

Where the auditor issues a review report on an engagement to review interim financial statements (in terms of ISRE 2410) and a reportable irregularity has been reported to the IRBA and the circumstances described in 14.2 above exist, the auditor should include a notification (or both a modified opinion and a notification) in his or her auditor's report on the annual financial statements in accordance with the requirements of section 44(2) and 44(3).

14.7 In Summary

Situation	Impact on auditor's report
Reporting process incomplete	Notification in the auditor's report (or both a modified opinion and a notification) *
Second report states reportable irregularity did not exist	No impact on auditor's report
Second report states reportable irregularity is no longer taking place and that adequate steps have been taken for the prevention or recovery of any loss as a result thereof	Notification in the auditor's report (or both a modified opinion and a notification) *
Second report states that reportable irregularity is continuing	Notification in the auditor's report (or both a modified opinion and a notification) *

*A notification that results from a reportable irregularity is included in the "Report on Other Legal and Regulatory Requirements" section of the auditor's report.

15 Unresolved/recurring reportable irregularities in subsequent years

- 15.1 The auditor will reassess the reportable irregularity for which the last auditor's report was modified before issuing any subsequent audit report. Where the prior year reportable irregularity is relevant to the current audit

of the financial statements, the auditor treats the reportable irregularity as a new reportable irregularity and complies with the provisions of section 45.

16 Withdrawal from the audit engagement

- 16.1 The ISAs and in particular ISA 240 and ISA 250 provide that the auditor may conclude that withdrawal from the engagement is necessary when the entity does not take the remedial action that the auditor considers necessary in the circumstances, even where the non-compliance or irregularity is not material to the financial statements.
- 16.2 The auditor must complete the reporting of a reportable irregularity before resigning from an audit. The report process is completed once the auditor has submitted the second report to the IRBA as required by section 45(3).
- 16.3 If an auditor suspects the existence of a reportable irregularity and the auditor is replaced (following resignation or a termination of services) such auditor should communicate the circumstances and details to the successor auditor in terms of section 210.13 of the IRBA Code.

Part 4 – Professional responsibility, disciplinary measures and other sanctions

17 Consequences for the auditor for failing to report a reportable irregularity

17.1 The auditor faces three possible consequences for failing to report a reportable irregularity as required by the APA

17.1.1 In terms of sections 48, 49, 50 and 51, the auditor may face investigation and disciplinary sanction by the IRBA – which sanction may include the following:

- a caution or reprimand to the auditor;
- a fine not exceeding the amount calculated according to the ratio for five year's imprisonment prescribed in terms of the Adjustment of Fines Act, 1991 (Act No. 101 of 1991)(presently R200,000);
- suspension of the right to practice as an auditor for a specific period;
and/or
- cancellation of the registration of the auditor concerned and removal of his or her name from the register of auditors.

17.1.2 In terms of section 46(7) of the APA, the auditor may incur liability to any partner, member, shareholder, creditor or investor of the entity if the auditor failed to report a reportable irregularity in accordance with section 45. Section 46(7), however, does not extend an unconditional right to any party to make such claim for damages. Only those parties able to prove the necessary elements of the delictual action for breach of statutory duty including the requirements of loss and causation may have such rights.

17.1.3 Section 52 of the APA deals with **reportable irregularities and false statements in connection with audits** and provides as follows:

- *“A registered auditor who-*
 - *fails to report a reportable irregularity in accordance with section 45; or*
 - *for the purposes of, or in connection with, the audit of any financial statement knowingly or recklessly expresses an opinion or makes a report or other statement which is false in a material respect, shall be guilty of an offence.*

- *Where the registered auditor failing to report a reportable irregularity or conducting the audit is a firm, subsection (1) applies to [the] individual registered auditor referred to in section 44(1)(a), but nothing in this subsection prevents the taking of disciplinary action under Chapter V in respect of the firm concerned, in addition to or instead of the individual registered auditor referred to in section 44(1)(a)*
- *A person convicted of an offence in a court of law under this section is liable to a fine or to imprisonment for a term not exceeding 10 years or to both a fine and such imprisonment”.*

18 Consequences for a registered audit firm for failing to report a reportable irregularity

18.1 The registered audit firm may face the following if the auditor fails to report the reportable irregularity:

- In terms of section 46(7) read with section 46(1) of the APA, the registered audit firm may face a civil claim for damages by any partner, member, shareholder, creditor or investor of the entity aggrieved by the reportable irregularity, if this was not reported, and a duty to report was owed. Section 46(7), however, does not extend an unconditional right to any party to make such claim for damages. Only those parties able to prove the necessary elements of the delictual action for breach of statutory duty including the requirements of loss and causation may have such rights.

19 Statutory protection for auditors

19.1 There is no statutory protection for an auditor if it is proved that the opinion was expressed, or the report or statement made, maliciously, fraudulently or pursuant to a negligent performance of the auditor`s duties.

20 Monitoring of compliance with section 45 of the APA

20.1 The IRBA monitors compliance with section 45 as part of its inspections at both firm and engagement level as appropriate. As part of the firm inspection, inspectors determine whether the firm has developed and implemented appropriate policies and procedures that are to be followed by all of its partners and personnel in the identification, reporting and managing of reportable irregularities. Inspectors also select a sample of reportable irregularities that were submitted to the IRBA to determine if all the requirements of section 45 have been complied with. Any non-

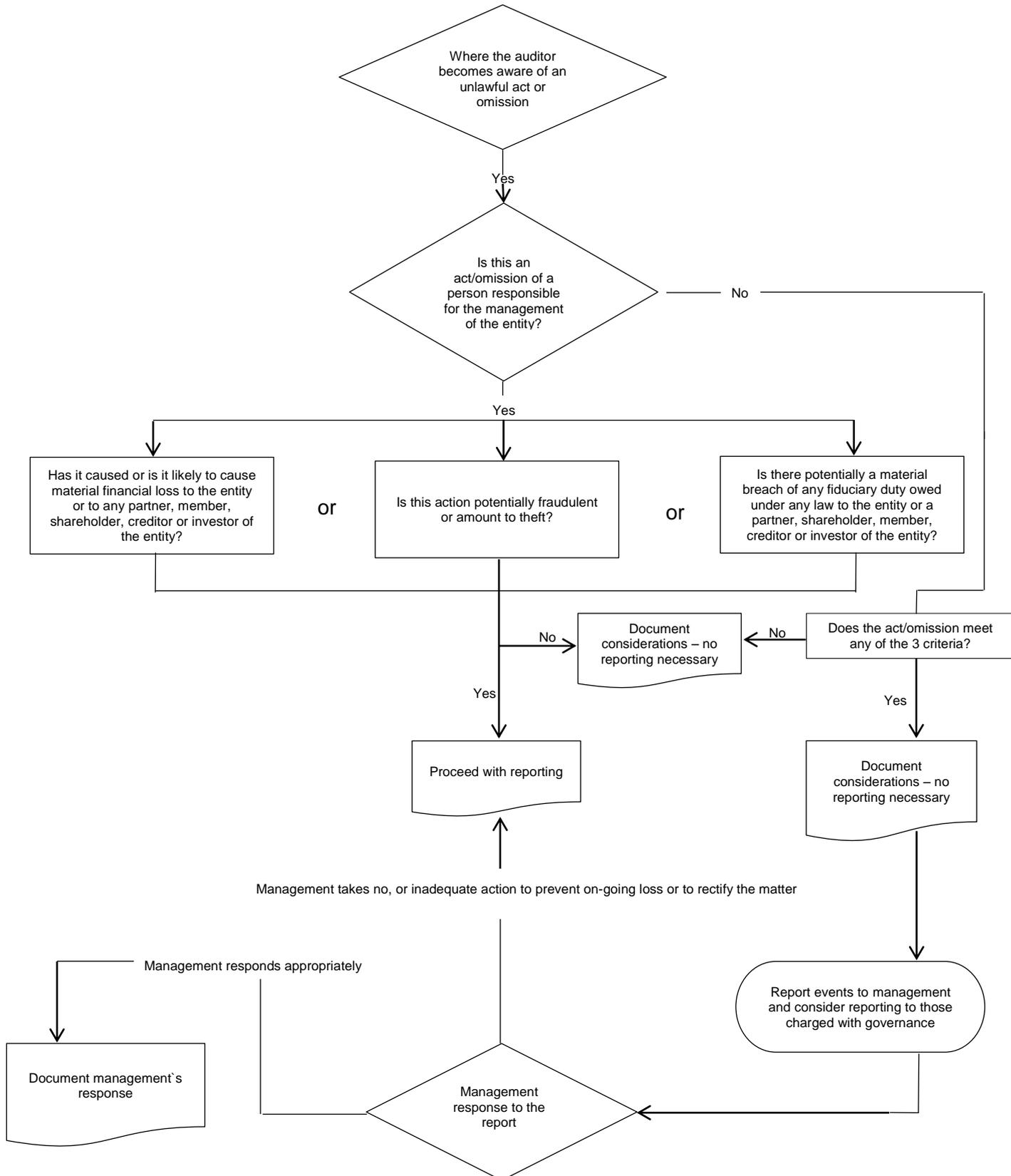
compliance of the firm with its own policies and procedures could be raised as inspection findings.

20.2 On engagements selected for inspection, the inspectors look out for any matters that may have arisen during the course of the audit that could indicate a possible reportable irregularity. These are followed up through discussion with the relevant practitioner and/or the inspection of any documented evidence of considerations and conclusions on the audit file to determine whether all the requirements of section 45 have been complied with.

20.3 The absence or lack of sufficient and appropriate documented considerations and determination on file whether a matter does/does not constitute a reportable irregularity, in itself, will normally result in an inspection finding being raised.

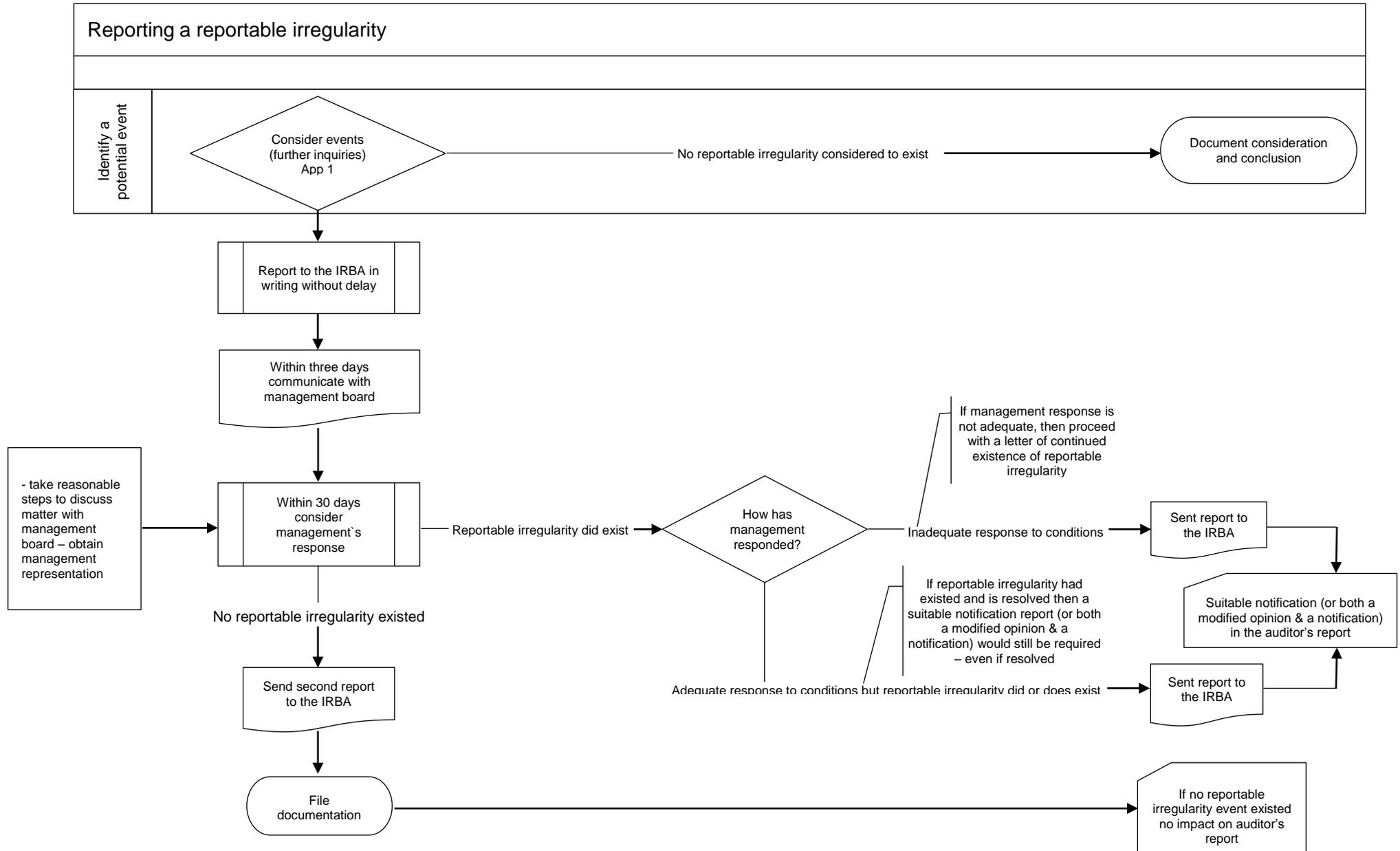
20.4 Inspectors also inspect whether the auditor's report is appropriate in the circumstances, for example, the inclusion of an appropriate notification as a separate paragraph under "Report on Other Legal and Regulatory Requirements" (detailing the reportable irregularity).

Appendix 1: A Diagrammatic presentation to determine whether an Irregularity is Reportable¹⁵



¹⁵ Note: The above diagrammatic presentation is not a substitute for considering and applying the relevant legislation

Appendix 2: A Diagrammatic presentation of the Process for Dealing with potential Reportable Irregularities



Appendix 3: Illustrative Auditor's First Report to the IRBA

Illustrative first report to the IRBA

<Firm letterhead>

<Date>

The Director: Standards
Independent Regulatory Board for Auditors
PO Box 8237
Greenstone
1616

Building 2
Greenstone Hill Office Park
Emerald Boulevard
Modderfontein
1609

Email: ristandards@irba.co.za

Telephone: 087 940 8800

Dear Sir

FIRST REPORT: REPORTABLE IRREGULARITY¹⁶

Name of entity audited: <Insert>

Registration number of entity: <Insert>

My firm has been engaged by <insert name of audited entity> to:

[Delete if not applicable]

1. Audit the company's annual financial statements.
2. Audit the entity's financial statements with the objective of expressing an opinion as to their fairness with an identified financial reporting framework.
3. Audit financial and other information, prepared in accordance with suitable criteria, with the objective of expressing an opinion on the financial and other information.

I have reason to believe that a reportable irregularity, as defined in the APA, has taken, or is taking place. I am not able to make a legal determination in respect of the suspected unlawful act or omission, but have exercised professional judgement, based on the evidence or information which has come to my attention, including undertaking further investigations of information as were considered necessary in the circumstances.

Particulars of the reportable irregularity are:

<Provide particulars, including any other information and particulars considered appropriate>.

¹⁶ For guidance on joint audits refer to paragraph 6.2 of the Guide

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Please acknowledge receipt of this report.

Yours faithfully

<Signature of registered auditor>

<Name of registered auditor>¹⁷

Registered Auditor

<Registered Auditor's IRBA registration number>

<Registered Auditor's direct email address>

<Registered Auditor's direct telephone number>

¹⁷ The registered auditor that submits this report should be the registered auditor responsible and accountable for the audit as determined in accordance with section 44(1) of the Auditing Profession Act.

Appendix 4: Illustrative Auditor's Letter to the Management Board of the Entity

Illustrative Letter to the Management Board of the Audited Entity

<Firm letterhead>

<Date>

Members of the management board

<Name of entity>

<Address>

Dear Members

REPORTABLE IRREGULARITY

This letter is issued in accordance with the requirements of the Auditing Profession Act, No. 26 of 2005, (the APA), section 45 – *Duty to report on irregularities*.

The APA defines a reportable irregularity as any unlawful act or omission committed by any person responsible for the management of an entity, which -

- (a) has caused or is likely to cause material financial loss to the entity or to any partner, member, shareholder, creditor or investor of the entity in respect of his, her or its dealings with the entity; or
- (b) is fraudulent or amounts to theft; or
- (c) represents a material breach of any fiduciary duty owed by such person to the entity or any partner, member, shareholder, creditor or investor of the entity under any law applying to the entity or the conduct or management thereof.

I have reason to believe that a reportable irregularity has taken or is taking place and, as required by the APA, I have reported particulars of the irregularity to the Independent Regulatory Board for Auditors (IRBA) in a written report dated <insert date> a copy of which is attached. As indicated in that letter, I am not able to make a legal determination in respect of the suspected unlawful act or omission, but have exercised professional judgement, based on the evidence or information which has come to my attention, including undertaking further investigations of information as were considered necessary in the circumstances.

The APA requires me as soon as is reasonably possible, but no later than 30 days from the date of the individual auditor's report which was forwarded to the IRBA, to send another report to the IRBA which must include:

1. A statement that I am of the opinion that:
 - (1) no reportable irregularity is taking place; or
 - (2) the suspected reportable irregularity is no longer taking place and that adequate steps have been taken for the prevention or recovery of any loss as a result thereof, if relevant; or
 - (3) the reportable irregularity is continuing.]
2. Detailed particulars and information supporting the statement above.

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Please note that, where the reportable irregularity is continuing, the IRBA has a responsibility to notify any appropriate regulator in writing of the details of the reportable irregularity and to provide it with a copy of my report.

I invite you to discuss my report to the IRBA, at a meeting to be arranged as soon as possible, and at that meeting I will afford you the opportunity to make representations in respect of my report.

Please acknowledge receipt of this report.

Yours faithfully

<Signature of registered auditor>

<Name of registered auditor>¹⁸

Registered Auditor

<Registered Auditor's IRBA registration number>

<Registered Auditor's direct email address>

<Registered Auditor's direct telephone number>

¹⁸ The registered auditor that submits this report should be the registered auditor responsible and accountable for the audit as determined in accordance with section 44(1) of the Auditing Profession Act.

Appendix 5: Illustrative Auditor's Second Report to the IRBA

Illustrative second report to the IRBA

<Firm letterhead>

<Date>

The Director: Standards
Independent Regulatory Board for Auditors
PO Box 8237
Greenstone
1616

Building 2
Greenstone Hill Office Park
Emerald Boulevard
Modderfontein
1609

Email: ristandards@irba.co.za

Telephone: 087 940 8800

Dear Sir

SECOND REPORT: REPORTABLE IRREGULARITY

Name of entity audited: <Insert>

Registration number of entity: <Insert>

I refer to my report of <insert date of initial report>.

I have included a copy of the written notice which was sent together with the abovementioned report to the members of the management board of the entity within three days of my having sent the first written report to you.

I have discussed that report with the members of the management board and have afforded them an opportunity to make representations in respect of the report. I have also undertaken such further investigations as I considered necessary.

I have included written representations made by members of the management board of the entity in respect of the report. [Delete if not applicable]

[OR]

Although I have taken all reasonable measures to communicate with the management board in respect of the suspected reportable irregularity, the board has failed or declined to engage in discussions with me. <However, I have undertaken such further investigations as I considered necessary. / I have also been unable to undertake such further investigations as I considered necessary>. [Delete whichever sentence is not applicable].

I report that in my opinion <no reportable irregularity has taken place or is taking place / the reportable irregularity is no longer taking place and that adequate steps

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have been taken for the prevention or recovery of any loss as a result thereof, if relevant / the reportable irregularity is continuing>. [Delete whichever is not applicable]

Details and information in support of my statement above are as follows:

<Provide details and information>

Contact details of the entity:

- <Insert title of person that can be contacted e.g. the CFO>
- <Insert name of contact person>
- <Insert telephone number of contact person>
- <Insert email address of contact person>

Please acknowledge receipt of this report.

Yours faithfully

<Signature of registered auditor>

<Name of registered auditor>¹⁹

Registered Auditor

<Registered Auditor's IRBA registration number>

<Registered Auditor's direct email address>

<Registered Auditor's direct telephone number>

¹⁹ The registered auditor that submits this report should be the registered auditor responsible and accountable for the audit as determined in accordance with section 44(1) of the Auditing Profession Act.

Appendix 6: Failing to Report a Reportable Irregularity

1. The paragraphs below are extracts from a legal opinion sought on the auditor's liability for failure to report a reportable irregularity, even though the audit was performed in terms of auditing standards.
 - 1.1 The discussion on this topic relates only to the category of reportable irregularity in which the auditor "has reason to believe" that such conduct has taken place. If the auditor is "satisfied" that a reportable irregularity has taken place, there is a mandatory reporting obligation, and failure to report constitutes an offence in terms of Section 52(1)(a). This follows from the unambiguous wording of Section 45(1)(a) which applies the subjective criteria that it is the individual auditor "that is satisfied". (See the discussion below).
 - 1.2 The phrase "has reason to believe" has been the subject of interpretation by South African courts in many cases dealing with criminal and administrative process, insolvency legislation and in cases dealing with the grounds justifying an order that security be given. In Vumba Intertrade CC v Geometric Intertrade CC 2001 (2) SA 106(A) Cloete J summarised the position as follows:

"Although the phrase 'there is reason to believe' places a much lighter burden of proof on an applicant than, for instance, 'the court is satisfied', the 'reason to believe' must be constituted by facts giving rise to such belief and a blind belief, or a belief based on such information or hearsay evidence as a reasonable man ought or could not give credence to, does not suffice.

In short, there must be facts before the court on which the court can conclude that there is reason to believe that a plaintiff close corporation will be unable to satisfy an adverse costs order; and the onus of adducing such facts rests upon the applicant." (We have omitted the intervening case reference citations in this passage).
 - 1.3 The subjective nature of the wording of Section 45(1)(a) – i.e. "an individual registered auditor ... of an entity that ... has reason to believe that a reportable irregularity has taken place" is clear insofar as it imposes a reporting obligation on an auditor who has such belief. The issue which is more complicated is whether it is necessary or appropriate to contemplate

the imposition of criminal sanctions on an auditor who was aware of a set of facts which ought reasonably to have led him/her to the belief that a reportable irregularity had occurred but who subjectively did not reach that conclusion by virtue of his/her negligence. The imposition of criminal sanctions based upon the subjective actual belief by an auditor and the deliberate failure to report represents a clear and unambiguous interpretation of the statute and would accord with the obvious intention of the legislature in introducing this new substantial penalty stipulation. The issue is whether the phrase is properly capable of interpretation to include the situation in which the auditor ought to have believed but did not subjectively so believe. The extension of a penalty in respect of negligent conduct would generally not be inferred in the absence of a clear indication to the contrary or in order to give proper effect to the obvious intention of the legislature. As Kellaway states in his book "Principles of Legal Interpretation" at page 236:

"A South African Court has clearly stated the principle that where a section of a penal enactment is capable of a reasonable interpretation which will avoid the penalty in any particular case, a court should adopt that construction."

- 1.4 In White v White and another (2001) 2 AER 43 the House of Lords was required to interpret the provisions of an industry based insurance agreement which was in turn intended to apply the stipulations of an EEC directive. In considering the interpretation of the phrase "knew or ought to have known" Lord Nicholls stated:

"Against this background I turn to the interpretation of the phrase 'knew or ought to have known' in cl 6(1)(e) of the 1988 MIB agreement. This question of interpretation is governed by English law. 'Ought' imports a standard by reference to which conduct is measured. Such is the prevalence of negligence in English law that the phrase immediately prompts the thought that the standard imported by 'ought' is the standard of the reasonable person. In cases of professional negligence the standard is that of the reasonably competent and careful professional in the relevant discipline. But this is not necessarily the standard. The meaning of the phrase depends upon its context. Here the context is the directive. The MIB agreement was entered into with the specific intention of giving effect to the directive."

- 1.5 Having concluded that the provision in the industry agreement ought to be restrictively interpreted, Lord Nicholls continued:

“The phrase ‘knew or ought to have known’ in the MIB agreement was intended to be co-extensive with the exception permitted by art 1 of the directive. It was intended to bear the same meaning as ‘knew’ in the directive. It should be construed accordingly. It is to be interpreted restrictively. ‘Ought to have known’ is apt to include knowledge which an honest person who enters the vehicle voluntarily would have. It includes the case of a passenger who deliberately refrains from asking questions. It is not apt to include mere carelessness or negligence. A mere failure to act with reasonable prudence is not enough. Hence it does not embrace the present case.”

- 1.6 In a dissenting judgment in the same case Lord Scott referred to this notion of a party deliberately refraining from acquiring a knowledge or belief when he quoted a previous judgment of his in which he sought to express the essentials of what he termed “blind-eye” knowledge as follows:

“Blind-eye knowledge requires, in my opinion, a suspicion that the relevant facts do exist and a deliberate decision to avoid confirming that they exist. The deliberate decision must be a decision to avoid obtaining information of facts in whose existence the individual has good reason to believe.”

- 1.7 It was this type of knowledge that was the basis of the earlier conclusion by Lord Nicholls that:

“The law generally treats this state of mind as having the like consequences as would follow if the person, in my example the passenger, had acted honestly rather than disingenuously. He is treated as though he had received the information which he deliberately sought to avoid. In the context of the directive that makes good sense. Such a passenger as much colludes in the use of an uninsured vehicle as a passenger who actually knows that the vehicle is uninsured. The principle of equal treatment requires that these two persons shall be treated alike.”

- 1.8 A court would restrictively interpret the provisions of Section 45(1)(a) as read with Section 52(1)(a) to hold that there has been a criminal offence in the case of an auditor who is subjectively satisfied or who subjectively has reason to believe or who, in the above sense, has “blind-eye” knowledge – i.e. who deliberately elects not to pursue an enquiry in order to avoid

obtaining confirmation of the facts which he suspects would give him reason to believe that a reportable irregularity has taken place. It is not believed that a court would interpret the statute as imposing criminal sanctions on an auditor who bona fide but negligently does not draw the conclusion that a reportable irregularity has occurred from facts discovered (even if a reasonably prudent auditor in his position would have done so) or who does not discover the facts in the first place (even if he ought to have done so by the exercise of reasonable care).

2. In summary:

Section 45 only imposes an additional regulatory reporting requirement on the auditor. The auditor is required to conduct his/her audit in accordance with the standards set out in the definition of “auditing pronouncements” and if he acts in accordance with those standards and fails to identify a reportable irregularity, then, absent particular factual circumstances, it ought not to be concluded that he acted negligently and certainly not that he acted in a manner subject to criminal or civil sanction. If the auditor acted bona fide but negligently in the sense discussed in 1.8 above, there may be civil consequences for the auditor and the firm under section 46(7) in appropriate cases, but criminal sanctions ought not to follow.

3. In addition, the auditor should also refer to sections 17 and 18 of this Guide that deals with consequences for the auditor and/or the registered audit firm for failing to report a reportable irregularity.

Appendix 7: Examples which illustrate application of the Guidance in determining the Existence of a Reportable Irregularity

These examples are not guidance in themselves, but should be considered as illustrative of the application of the guidance provided in this Guide and the auditor should consult the Guide in each circumstance. The examples provided are not intended to be exhaustive nor prescriptive but rather serve to illustrate the kinds of acts or omissions which may give rise to reportable irregularities, depending on the particular facts and circumstances. Auditors should apply their professional judgement to the specific facts and circumstances presented in each case.

Good practice would suggest auditors consider and adequately document their considerations or thought process as outlined in the first illustrative example. Further, auditors may wish to seek legal advice in specific circumstances.

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APPENDIX 7: EXAMPLES WHICH ILLUSTRATE APPLICATION OF THE GUIDANCE IN DETERMINING THE EXISTENCE OF A REPORTABLE IRREGULARITY

	Is this an act of a person responsible for the management of the entity?	Is this an unlawful act or omission?	Does this meet ANY of the following conditions: 1. Caused / likely to cause material financial loss 2. Fraudulent or amounts to theft 3. Material breach of fiduciary duty	Is this a reportable irregularity?
1	A company has failed to prepare annual financial statements within six months of its financial year end.			
	Yes, in terms of section 66(1) of the Companies Act the directors are responsible for management of the company, which includes the preparation of financial statements. One of the key functions of the board is to approve the annual financial statements (section 30(3)).	Yes, this is in contravention of section 30 of the Companies Act which requires that a company must prepare annual financial statements within six months after the end of its financial year.	This example demonstrates the nature of considerations which should be undertaken before deciding whether a set of facts and circumstances constitute a reportable irregularity. Please see analysis below.	Possibly.

Considerations:

What additional qualitative factors may be considered in order to determine whether the unlawful act/omission meets the definition of a reportable irregularity?

(a) has caused or is likely to cause material financial loss to the entity or to any partner, member, shareholder, creditor or investor of the entity in respect of his, her or its dealings with that entity?

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- Do the draft annual financial statements (or accounting records) reflect material operating losses or liquidity problems such that the company would breach external debt covenants and an external financier or other creditor with right of access to the financial statements may incur material financial loss as a result of withholding the information?
- Is the company listed on a stock exchange and, in the absence of financial information, shareholders may make inappropriate trading decisions and incur material financial loss as a result of withholding the information?
- Is the company liable for material administrative fines from the Companies Intellectual Property Commission (CIPC) due to the non-compliance (applicable if a compliance notice issued by CIPC has been ignored in terms of s171(7))?
- Have all shareholders, including minority shareholders, obtained appropriate access to alternative financial information that is not materially different to the information presented in the annual financial statements, such that there is little risk of their decision making having been impeded by the delay?
- Is the company a public interest entity, as defined in the IRBA Code? In the absence of financial information, investors and creditors may make inappropriate decisions and incur material financial loss as a result of the information being withheld?

(b) is fraudulent or amounts to theft?

- Is the Board of the company purposely withholding the annual financial statements in order to conceal fraud or theft?

(c) represents a material breach of any fiduciary duty owed by such person to the entity or any partner, member, shareholder, creditor or investor of the entity under any law applying to the entity or the conduct or management thereof?

The mere failure to comply with section 30 of the Companies Act does not by itself amount to a breach of fiduciary duty. However, the attitude of the director's and their reasons and motivation to act or fail to act in a certain way, and the consequences of their actions or inaction for the company, may amount to a material breach of fiduciary duty. The directors must promote and protect the interests of the company. The directors' failure to ensure that annual financial statements were prepared within six months of the company's financial year end could raise concerns whether the directors have exercised their powers for a proper purpose in the circumstances and whether they have acted in good faith. The consideration of these matters requires additional information about the surrounding circumstances. The following factors may be relevant:

- Is the company actively trading or is the company dormant?

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- Do the shareholders already have access to relevant financial information for the financial accounting period through management accounts (e.g. if the company is a wholly owned subsidiary and the parent company receives a reporting pack)?
- Are there other instances of legislative or regulatory non-compliance which suggests a pattern of conduct, for example outstanding tax returns/overdue filings and/or disputes with tax authorities?
- Has the company complied with stock exchange requirements to inform shareholders of the reasons for the delay (where applicable)?
- Is there a history of late preparation of the annual financial statements, or is this the first year in which these annual financial statements are late?
- How long outstanding are the annual financial statements?
- Are there other annual financial statements within the Group which are also late, where the same management is responsible? This may indicate an attitude of non-compliance by management.
- Is the reason for the delay in the annual financial statements due to a factor that, despite management's best efforts, is beyond its control? e.g. the finalisation of the company's annual financial statements depends on material information that is outstanding from an offshore related company. Management has made every effort to obtain the information from the related company.
- Is there an apparent wilful disregard for the law?
- Have management implemented appropriate processes and applied adequate resources which, were it not for the extenuating circumstances, would have had reasonable prospects to achieve compliance with the law?
- Does the company have external debt and do the external financiers have a right of access to the annual financial statements?

Conclusion:

Depending on the facts and circumstances, the auditor may conclude that there is a reportable irregularity.

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	Is this an act of a person responsible for the management of the entity?	Is this an unlawful act or omission?	Does this meet ANY of the following conditions: 1. Caused / likely to cause material financial loss 2. Fraudulent or amounts to theft 3. Material breach of fiduciary duty	Is this a reportable irregularity?
2	A company paid out incentive bonuses on the instruction of the Human Resources (HR) Director, but failed to deduct Pay As You Earn (PAYE) taxes. It was subsequently discovered by the company and the correct PAYE, including penalties and interest, was paid over to SARS and the PAYE was recovered from the staff. The penalties and interest were not material.			
	<p>Who committed the act?</p> <p>(a) If the payroll accountant neglected to make the PAYE deductions without the knowledge of the HR Director, then the act was not committed by a person responsible for the management of the entity.</p> <p>(b) If the decision not to deduct PAYE was made on the instruction of, or with the knowledge of the HR director, then the act was committed by a person responsible for the management of the entity. "Director" means member of the board. In terms of section 66(1) of the Companies Act the director is responsible for the management of the company which will reasonably include, in the context of the functions of the HR</p>	Yes, this is an unlawful act or omission as failing to deduct PAYE on time is a contravention of the Income Tax Act.	<p>Refer to scenario (a) in the 1st column: It is not necessary to consider any of these conditions, since the act was not committed by a person responsible for the management of the entity.</p> <p>Refer to scenario (b) in the 1st column: It has not resulted in a material financial loss to SARS in its dealings with the company as SARS did ultimately receive the correct amount.</p> <p>It has also not resulted in a material loss to the company as the interest and penalties were not material to the company in its dealings with SARS.</p> <p>Unless there is evidence that the actions of the director were intentional, this</p>	<p>Scenario (a) No.</p> <p>Scenario (b) Possibly. <u>(Note:</u> The fact that the company had already corrected the error does not remove the obligation on the auditor to consider whether, based on the specific circumstances, a reportable irregularity</p>

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	director, to ensure that the company complies with the Income Tax Act.		would not amount to fraud or theft. The director does not owe a fiduciary duty to SARS. Instead, the company has a statutory obligation to deduct and remit PAYE in terms of the Income Tax Act. Therefore this is not a material breach of fiduciary duty. However, if the failure to deduct PAYE is a recurring problem, this may be an indication of a material breach of fiduciary duty owed to the company.	exists).
3	Income tax returns or other tax returns that are incomplete in a material respect.			
	If management was aware of or directly responsible for the non-compliance, it will be an act or omission by management as they should ensure that the company complies with its obligations in terms of the relevant tax legislation.	Yes, an incorrect/incomplete return submitted is a contravention of the relevant Tax legislation.	If the amount of additional taxes, penalties and interest is material in relation to SARS in its dealings with the company, the auditor would conclude that the unlawful act or omission either has caused or is likely to cause material financial loss to SARS and/or the company.	Possibly.

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	Is this an act of a person responsible for the management of the entity?	Is this an unlawful act or omission?	Does this meet ANY of the following conditions: 1. Caused / likely to cause material financial loss 2. Fraudulent or amounts to theft 3. Material breach of fiduciary duty	Is this a reportable irregularity?
			<p>Unless there is evidence that the actions of the director(s) were intentional, this would not amount to fraud or theft.</p> <p>The directors do not owe a fiduciary duty to SARS. Instead, the company has a statutory obligation to prepare and submit all tax returns which are due accurately. Therefore this is not a material breach of fiduciary duty.</p> <p>However, if the failure to complete tax returns appropriately is a recurring problem, this may be an indication of a material breach of fiduciary duty owed to the company.</p>	
4	A company is involved in activities for which the tax treatment is uncertain. As a result, management utilised advice from an independent tax specialist in completing its income tax return, and such advice was bona fide. However, SARS disagreed with the treatment and ruled that the Income tax return was incomplete in a material respect.			
	Yes. As management was aware of or directly responsible for the tax treatment adopted in the return, it will be an act or omission by management as they should	No. As the Income Tax Act was not clear in this respect and the tax return was completed on the basis of	Even if there was a material financial loss to SARS it would not be relevant since there has been no unlawful act or omission.	No.

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	Is this an act of a person responsible for the management of the entity?	Is this an unlawful act or omission?	Does this meet ANY of the following conditions: 1. Caused / likely to cause material financial loss 2. Fraudulent or amounts to theft 3. Material breach of fiduciary duty	Is this a reportable irregularity?
	ensure that the company complies with its obligations in terms of the Income Tax legislation.	bona fide professional advice, management has not intentionally contravened the relevant Tax legislation or acted negligently. See also Section 76(5) of the Companies Act.	The return had been completed in good faith on the basis of bona fide professional tax advice, and this would not amount to fraud or a material breach of fiduciary duty.	
5	Late submission and payment of VAT returns, where the amount owing (with or without resultant penalties or interest) is not material.			
	If management was aware of or directly responsible for the non-compliance, it will be an act or omission by management, as they have to ensure that the company complies with its obligations in terms of the Value Added Tax Act (VAT Act).	Yes, the late submission and payment of returns is a contravention of the VAT Act.	Neither SARS nor the company has suffered a material financial loss. In the absence of evidence that the company acted intentionally, this would not amount to theft or fraud. Management /the directors does/do not owe a fiduciary duty to SARS and therefore there has not been a material breach of fiduciary duty. However, if the late submission of VAT returns is a recurring problem, this may be an indication of a material breach of	Possibly.

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	Is this an act of a person responsible for the management of the entity?	Is this an unlawful act or omission?	Does this meet ANY of the following conditions: 1. Caused / likely to cause material financial loss 2. Fraudulent or amounts to theft 3. Material breach of fiduciary duty	Is this a reportable irregularity?
			fiduciary duty owed to the company.	
6	During the audit it was identified that the company did not submit VAT returns and did not make payments in respect thereof to SARS. The company is experiencing cash flow problems and is finding it difficult to obtain finance.			
	The auditor needs to determine whether management was aware of or directly responsible for the non-compliance. Even if the person who submits the returns and related payments is not a person responsible for management of the entity, the auditor should consider whether management would reasonably be expected to know about the late submissions (e.g. through normal internal control processes or internal audit activity).	Yes, non-submission of the VAT returns and non-payment thereof is a contravention of the VAT Act.	Yes, depending on the facts and circumstances. The non-compliance may give rise to a material financial loss to SARS in its dealings with the company. If there was any intentional misrepresentation by management in the form of incomplete returns or in any other way, this may amount to fraud. Directors do not owe a fiduciary duty to SARS. The company has a statutory obligation to submit its VAT returns and settle its VAT liabilities. However, management should not exercise its powers for an improper purpose and should deal with the company openly and in good faith. Depending on management's attitude and motivation, trends in non-compliance	Possibly. The auditor should also consider whether the company is in financial distress, as the company is experiencing cash flow problems.

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	Is this an act of a person responsible for the management of the entity?	Is this an unlawful act or omission?	Does this meet ANY of the following conditions: 1. Caused / likely to cause material financial loss 2. Fraudulent or amounts to theft 3. Material breach of fiduciary duty	Is this a reportable irregularity?
			and the impact and consequences of non-compliance, such an intentional act by management may amount to a material breach of fiduciary duty owed to the company.	
7	During the audit it is identified that a branch of the company has failed to make a payment to a third party of amounts withheld on that party's behalf – often Pension Fund Contributions or Medical Aid Contributions. The person responsible for these payments is the Branch Financial Manager. Management of the company is aware of these non-payments but does not take action to pay over the amounts in question to the ultimate intended recipient.			
	The Branch Financial Manager would probably not be seen as a person responsible for the management of the company, since his/her decisions do not extend to the organisation as a whole. The auditor should consider whether there is any basis to suggest that the branch Financial Manager is a prescribed officer of the company, in which case he/she will be seen as a person responsible for management of the company (see paragraph 3.1.3 of the	In the case of some payments (e.g. Pension Fund contributions) this would be an unlawful act or omission. A deliberate breach of a contractual obligation is unlawful.	Yes, if it assumed that the non-payments and the resulting interest and penalties are material, the omission gives rise to a material financial loss to fiscal authorities and/or others (creditors and employees). Furthermore, management's failure to take action to address the non-compliance may constitute fraud as management's failure to act may indicate intent to mislead and/or deceive. Depending on the impact and consequences, this act by management	Possibly.

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	Is this an act of a person responsible for the management of the entity?	Is this an unlawful act or omission?	Does this meet ANY of the following conditions: 1. Caused / likely to cause material financial loss 2. Fraudulent or amounts to theft 3. Material breach of fiduciary duty	Is this a reportable irregularity?
	Guide). However, in this case it is stated that “management of the company is aware of these non-payments”. This will be regarded as an omission by a person responsible for the management of the entity.		may amount to a material breach of a fiduciary duty owed to the company. The non-payment of the correct amounts could cause the third parties to institute legal action against the company, which may also cause reputational damage to the company. It should be questioned whether management has exercised its power for a proper purpose and has acted openly and in good faith.	
8	A Financial Director misappropriated funds and it was discovered by the company. He was summarily dismissed, criminally charged and the misappropriated funds have been recovered.			
	Yes. The financial director, as a member of the board of directors, will be seen as a person responsible for the management of the entity.	Yes. The misappropriation of funds is unlawful.	Although the funds have been recovered, the unlawful act or omission was still committed and the recovery of the funds was a corrective action that was taken. The act was fraudulent and amounted to theft. Furthermore, this action amounts to a material breach of fiduciary duty as the Financial Director exercised his/her	Yes. Although the matter was adequately dealt with by management, a reportable irregularity did take place. The report to IRBA would include details of the remedies implemented

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			power for an improper purpose; did not deal with the company openly and in good faith; and instead took certain economic decisions for his/her benefit.	by management.
9	The auditor is engaged in an audit of the annual financial statements. During the fraud and error discussion with the CFO, the CFO disclosed to the auditor that the accounts clerk has committed fraud in an amount of R 135 000. Management's action was to dismiss the employee. This matter was not reported to the police.			
	Clearly the fraud involved was not committed by a person responsible for the management of the entity (i.e. the accounts clerk). The CFO also did not have prior knowledge of the fraud; once he/she found out about the fraud he/she acted against the accounts clerk. The omission that was committed by the CFO was not to report or cause the matter to be reported to the police. In this regard, the CFO is clearly a person responsible for the management of the company.	This is an unlawful act or omission as the audit client failed to comply with section 34 of the Prevention and Combating of Corrupt Activities Act (PRECCA). Section 34 of PRECCA requires that any person in a position of authority who knows or ought reasonably to have known or suspected that any other person has committed an offence under PRECCA or the offence of theft, fraud,	Failure to report such a matter to the police may result in a fine or imprisonment being imposed under PRECCA against the CFO. As such the imposition of the fine will not result in any material financial loss to the company. While the conduct of the accounts clerk undoubtedly amounted to theft or fraud, it was not a reportable irregularity because it was not committed by a person responsible for the management of the entity. Lastly the auditor would need to consider whether the CFO withheld details of the fraud by the accounts clerk	Possibly.

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	Is this an act of a person responsible for the management of the entity?	Is this an unlawful act or omission?	Does this meet ANY of the following conditions: 1. Caused / likely to cause material financial loss 2. Fraudulent or amounts to theft 3. Material breach of fiduciary duty	Is this a reportable irregularity?
		extortion, forgery or uttering a forged document involving an amount of R 100 000 or more must report such knowledge or suspicion, or cause it to be reported to any police official.	from the other directors and therefore did not deal with the company openly and in good faith. If this was the case, the CFO's action may amount to a material breach of fiduciary duty.	
10	A bribe was paid by a salesman of a foreign subsidiary in order to obtain a key government contract in that country. The salesman was instructed to pay the bribe by the Sales and Marketing Director of the South African parent company.			
	Yes, since it was done with the knowledge of or on the instruction of a director (the sales and marketing director) who is a person responsible for the management of the company. However, if the bribe had been paid by the foreign subsidiary without the knowledge of South African management, the obligation under the APA for the auditor to report a reportable irregularity would not arise.	Yes, it constitutes an offence of corruption as contemplated in PRECCA.	Yes, this act amounts to fraud as the director's actions were intentionally deceitful and corrupt. Furthermore, this action amounts to a material breach of fiduciary duty as the director exercised his powers for an improper purpose by instructing the salesman to commit a criminal act and by influencing a third party through a gratification payment to act with bias.	Yes. The auditor should also consider whether the directors have an obligation to report the bribe to FICA.
11	A company's Memorandum of Incorporation (MOI) states that a minimum of 80% of directors must be present at a meeting of the directors before a vote may be called. In the current financial year, one out of the six board meetings held in the year was held with only 70% of directors present.			

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	The notice of the meeting was duly circulated to all directors beforehand, but 30% of the directors were unable to be present at this meeting.			
	Yes as the directors are responsible for ensuring that the company is in compliance with the MOI. In terms of section 15(6) of the Companies Act, a company's MOI is binding between the company and each director of the company.	Yes, as the non-compliance with the provisions of the MOI is a contravention of section 15(6) of the Companies Act	Possibly. The consideration of material financial loss would depend on what matters were discussed and agreed at the meeting, for example the directors may have concluded to enter into a contract which could have the effect of causing a material financial loss to many parties. Since all of the directors were given due notice of the meeting, the non-compliance does not appear to be a deliberate act of management intended to cause prejudice and is accordingly not fraud or theft. Furthermore, there could be a material breach of fiduciary duty depending on what was agreed and the surrounding circumstances, for example they may have approved the provision of financial assistance to a director.	Possibly.

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	Is this an act of a person responsible for the management of the entity?	Is this an unlawful act or omission?	Does this meet ANY of the following conditions: 1. Caused / likely to cause material financial loss 2. Fraudulent or amounts to theft 3. Material breach of fiduciary duty	Is this a reportable irregularity?
			Depending on the directors' motivation and the impact and consequences of the transaction(s) that was(were) approved, questions could be raised around whether the directors have, in the circumstances, exercised their power for a proper purpose and whether they have acted openly and in good faith.	
12	A listed company which prepared its annual financial statements (AFS) in accordance with International Financial Reporting Standards (IFRS), failed to disclose key information regarding related parties. The engagement partner intends issuing a qualified auditor's report.			
	Yes, in terms of section 66(1) of the Companies Act the directors are responsible for management of the company, which includes the preparation of financial statements. One of the key functions of the board is to approve the annual financial statements (section 30(3)).	Yes, since section 29(4) of the Companies Act read with Regulation 27 requires listed companies to apply IFRS in the preparation of their annual financial statements.	It is unlikely that the non-compliance with the Companies Act could directly cause material financial loss, since the annual financial statements are to be issued together with an appropriately qualified auditor's report (the necessary information may be made available to the intended users through the auditor's report modification). If the non-disclosure of this information was intended to misrepresent the facts in	Possibly.

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	Is this an act of a person responsible for the management of the entity?	Is this an unlawful act or omission?	Does this meet ANY of the following conditions: 1. Caused / likely to cause material financial loss 2. Fraudulent or amounts to theft 3. Material breach of fiduciary duty	Is this a reportable irregularity?
			the AFS, then the omission would be fraudulent and most likely represent a reportable irregularity. Furthermore, the auditor should also refer to the considerations mentioned in the first illustrative example for additional guidance in determining whether or not there was a material breach of fiduciary duty.	
13	A listed company which prepared its annual financial statements (AFS) in accordance with International Financial Reporting Standards (IFRS) and the Companies Act, failed to disclose individual directors' remuneration as required by the Companies Act and the JSE Limited Listings Requirements (JSE Listings Requirements). The engagement partner intends issuing a qualified auditor's report.			
	Yes, in terms of section 66(1) of the Companies Act the directors are responsible for management of the company, which includes the preparation of financial statements. One of the key functions of the board is to approve the annual financial statements (section 30(3)).	Yes, since section 30 of the Companies Act and section 7.B.7 of the JSE Listings Requirements requires listed companies to disclose directors' remuneration.	It is unlikely that the non-compliance with the particular requirements could directly cause material financial loss, since the annual financial statements are to be issued together with an appropriately qualified auditor's report (the necessary information may be made available to the intended users through the auditor's report modification).	Possibly.

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			<p>If the non-disclosure of this information was intended to misrepresent the facts in the AFS, then the omission would be fraudulent and most likely represent a reportable irregularity.</p> <p>If this omission was intentional then this act would amount to a material breach of fiduciary duty as the directors should not exercise their powers for an improper purpose and should deal with the company openly and in good faith.</p> <p>Furthermore, the auditor should also refer to the considerations mentioned in the first illustrative example for additional guidance in determining whether or not there was a material breach of fiduciary duty.</p>	
14	<p>A company is experiencing difficulties in settling its debts in the normal course of business. However, management has indicated that they are negotiating a new business deal with a major customer and have approached a financial institution about extending its funding facilities. The directors are concerned that the company is financially distressed as defined in Chapter 6 of the Companies Act, but have not yet resolved to enter into business rescue proceedings.</p>			

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	<p>Yes. In terms of section 66(1) of the Companies Act the directors are responsible for management of the company. This includes policymaking and decision-making regarding the solvency and liquidity of the company, and ensuring that the company is not carrying on business recklessly or not trading under insolvent circumstances.</p>	<p>Possibly, since failing to enter into business rescue proceedings or to distribute the written notice required by section 129(7) to all affected parties where a company is financially distressed is a contravention of Chapter 6 of the Companies Act.</p> <p>The auditor would need to consider all available evidence to evaluate the directors' considerations about whether the company is financially distressed.</p> <p>Considerations such as the likelihood that a new business deal will be concluded (e.g. by considering past history of such deal negotiations) and whether management is likely</p>	<p>If the company is indeed financially distressed, continuing to trade without appropriate funding may cause material financial loss to many parties, including shareholders and creditors.</p> <p>Furthermore, this action amounts to a material breach of fiduciary duty, as the directors have a responsibility to deal with the company openly and in good faith and failing to apply for business rescue or inform the shareholders as set out in the Companies Act appears contrary to this.</p>	<p>Possibly.</p>

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		<p>to obtain the funding necessary to enable it to pay its creditors in the normal course of business, as and when they fall due.</p> <p>Furthermore, the auditor would typically also consider non-compliance with section 22 of the Companies Act.</p>		
15	<p>The auditor of a company has reasonable grounds to believe that the company is unable to pay its debts as they become due and payable in the normal course of business and it appears to be reasonably unlikely that the company will be able to pay all of its debts as they become due and payable within the immediately ensuing six months; or it appears to be reasonably likely that the company will become insolvent within the immediately ensuing six months. However, the directors disagree with the auditor's assessment and fail to comply with the requirements of section 128 and 129 of the Companies Act dealing with business rescue proceedings.</p>			
	<p>In terms of section 66(1) of the Companies Act the directors are responsible for management of the company. This includes policymaking and decision-making regarding the solvency and liquidity of the company, and ensuring that the company is not</p>	<p>Possibly. The directors are responsible for decision-making regarding the solvency and liquidity of the company, including ensuring that the company is not trading under insolvent circumstances and</p>	<p>Possibly. If the company is unable to pay its debts as they become due and payable in the normal course of business and it appears to be reasonably unlikely that the company will be able to pay all of its debts as they become due and payable within the immediately ensuing</p>	<p>Possibly.</p>

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	<p>carrying on business recklessly or not trading under insolvent circumstances.</p>	<p>owes a duty of care toward the company. The directors should take all facts into consideration and carefully consider such facts when evaluating whether the company is financially distressed. If the directors fail to take all facts into consideration with due care in this evaluation they would probably be breaching their fiduciary duty and similarly fail to comply with the requirements of the Companies Act with respect to entering into business rescue proceedings (section 129), or concluding not to do so which would require compliance with section 129(7) by issuing the required written notice to each affected person. Therefore the</p>	<p>six months, or it appears to be reasonably likely that the company will become insolvent within the immediately ensuing six months it may cause material loss to many parties, including shareholders and creditors.</p> <p>Furthermore, this may amount to a material breach of fiduciary duty, as the directors have a responsibility to comply with the Companies Act with respect to assessing whether the company is financially distressed or not and whether the company should enter into business rescue proceedings and has a responsibility to act with due care toward the company in this regard.</p>	

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		auditor applies judgment in determining whether the directors have breached their fiduciary duty to comply with the Companies Act.		
16	A company's liabilities exceed its assets (i.e. it is technically insolvent). There is currently no indication that the company is not able to pay its debts as they fall due, and the company's holding company has subordinated its loan in favour of all other creditors until solvency is restored.			
	Yes. In terms of section 66(1) of the Companies Act the directors are responsible for management of the company. This includes policymaking and decision-making regarding the solvency and liquidity of the company, and ensuring that the company is not carrying on business recklessly or not trading under insolvent circumstances.	No, since it appears that the company is able to settle its debts and the holding company has subordinated its loan, therefore it appears that it has some financial support to continue to operate and accordingly does not appear to be in financial distress or carrying on business recklessly.	No, it does not appear that material financial loss will be caused to any party. Furthermore, depending on the actions of the directors, technical insolvency would not automatically amount to a breach of fiduciary duty, unless the directors have abused their powers or not acted in the best interests of the company.	No. However, if there is an indication that a company is unable to settle its debts and management is ignoring the situation and continuing to incur debts when there is a possibility they cannot be repaid, then a reportable irregularity exists. Section 22 of the

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				Companies Act prohibits a company from carrying on its business recklessly.
17	A parent company provides financial assistance to a subsidiary, after approval at the board meeting but without a special resolution approved by the shareholders, in order to assist the company to buy back non-controlling shares held by the directors of the subsidiary. Written notice was not provided to the parent company shareholders and trade unions. Immediately after providing the financial assistance, the parent company does not satisfy the solvency and liquidity test.			
	Yes. The financial assistance was approved by the board. The directors of a company are the persons responsible for the management of the entity.	Yes, since it is a contravention of section 45 of the Companies Act. In this case, financial assistance to a related or inter-related company.	Yes. The provision of financial assistance that has not followed a proper approval process may result in material financial loss to the company, since part of the objective of the approvals is to prevent a loss from occurring. The individual circumstances would need to be evaluated. The directors were aware of their responsibilities but chose not to follow the approval process to push a transaction through, this is an intentional act and hence fraudulent.	Yes.

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			Depending on the specific facts, a breach of fiduciary duty may exist, particularly if the actions of the directors were to endorse the transaction, since they may have used their powers for an improper purpose.	
18	Working capital was provided to a subsidiary in the normal course of business. The directors of the parent company approved the transaction, but omitted to obtain a special resolution authorising the provision of this financial assistance and did not perform a formal solvency and liquidity test as required by the Companies Act. However, the parent company is liquid and solvent.			
	Yes, since the directors must exercise their powers and perform the functions of director in good faith, for a proper purpose and in the best interest of the company.	Yes, since it is a contravention of section 45 of the Companies Act.	No, since the omission has not caused material financial loss to any party. There is no indication of any intentional act to mislead, deceive or conceal. Therefore no fraud or theft. As the parent company is liquid and solvent (and management are reasonably expected to be aware of this), the failure or oversight by the directors to perform the solvency and liquidity test and omitting to obtain a special resolution for providing authorisation to arrange working capital	No.

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			<p>funding in the normal course of business is not considered to be a material breach of fiduciary duty.</p> <p>However, the auditor also would need to consider whether management of the company habitually flouts the requirements of the Companies Act and whether this would constitute a material breach of fiduciary duty.</p>	
19	The auditor is engaged in an audit of annual financial statements. The company being audited did not maintain proper accounting records to substantiate material balances and totals in the financial statements.			
	Yes, in terms of section 66(1) of the Companies Act the directors are responsible for management of the company, which includes ensuring that proper accounting records are maintained in terms of section 28 of the Companies Act.	Yes, this is an unlawful act or omission as the company failed to keep accurate and complete accounting records as required by section 28 of the Companies Act.	<p>As in example one above, the auditor would be required to carefully consider the surrounding circumstances in order to decide whether a reportable irregularity exists or not.</p> <p>A reportable irregularity exists if this action or omission is likely to cause a material financial loss to the company or any of the other affected stakeholders as defined.</p>	Possibly.

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			<p>Depending on the intentions and motivation of the directors (e.g. to deliberately conceal inappropriate transactions or actions) this action may amount to fraud.</p> <p>Furthermore, this could amount to a material breach of fiduciary duty depending on the extent to which the records are unavailable. Maintaining proper accounting records is in the best interest of the company. They are necessary to enable the preparation of annual financial statements and form an integral part of a company's internal control to, amongst others, safeguard the company's assets and resources.</p>	
20	A listed company has failed to appoint a social and ethics committee.			
	Yes, the appointment of a social and ethics committee falls within the general ambit of the directors being responsible for the management of the company in	Yes, since the Companies Act (section 72 and Regulation 43 of the Companies Regulations) requires listed companies to	It is unlikely that the failure to appoint a social and ethics committee will cause material financial loss as defined. This act or omission does not amount to	Possibly.

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	terms of section 66(1) of the Companies Act.	appoint a social and ethics committee.	theft or fraud. A breach of the Companies Act does not necessarily equate to a breach of fiduciary duty. However, if the non-compliance is recurring then it would be a material breach of fiduciary duty.	
21	An audit client that conducts business as a financial advisor in terms of the Financial Advisory and Intermediary Services Act (FAIS Act) has failed to keep client funds in a separate bank account from the business account.			
	Yes, since the directors are responsible for the management of the entity and this would be expected to be a matter that receives attention at the directors' level.	Yes, since this is non-compliance with the FAIS Act.	Yes, since the co-mingling of trust monies with those of the business may have caused material financial loss to many parties. Where the trust monies have been used for business purposes, this could constitute theft or fraud. Furthermore, this action amounts to a material breach of fiduciary duty, as the directors have a fiduciary duty towards the trust creditors in respect of the funds	Yes.

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			placed in trust with the financial advisor and should not exercise their powers for an improper purpose.	
22	The auditor of a company that trades as an estate agent noted the following during the audit of the estate agents trust accounting records: The system had been circumvented in that not all cash received in respect of trust monies was banked and certain business expenses were paid from the trust account.			
	Additional information is required to make a determination in this regard. The directors are responsible for the management of the company, including the maintenance of proper trust accounting records and related internal control. A trust accounting system had been implemented, but it was circumvented. Therefore, the auditor has to consider who was involved in these actions. If the directors were directly involved, or the actions were performed on instruction of the directors or with their knowledge, this will amount to actions of a person responsible for the	Yes. It is a contravention of section 32 of the Estate Agents Affairs Board Act.	Yes, if these actions have caused or is likely to cause material financial loss to trust creditors. It is fraudulent as there was an unlawful and intentional appropriation of another's property. Furthermore, if this amounts to actions of a person responsible for the management of the entity (refer to the 1 st column), it is likely to be a breach of fiduciary duty as the directors have not acted in good faith in protecting the interests of the company and its clients. The nature of the breach (misappropriation of monies held in trust)	Possibly.

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	management of the entity.		is material.	
23	The managing agent of a body corporate (sectional title scheme) misappropriated funds from the entity's trust account, without the consent or knowledge of the board of trustees. You are the auditor of the body corporate.			
	<p>Yes, the board of trustees delegates its responsibility to the managing agent.</p> <p>The managing agent prepares the entity's annual budgets, chairs the Annual General Meeting and liaises with the auditors on all financial matters.</p> <p>Thus the managing agent is considered to be responsible for the management of the body corporate, although not a trustee of the entity.</p>	<p>Yes, since money held in trust was stolen (a criminal act).</p>	<p>Yes, material financial loss may have been caused to many parties.</p> <p>This act is fraudulent as there was an unlawful and intentional appropriation of another's property.</p> <p>Furthermore, these actions amount to a breach of fiduciary duty as the managing agent has not acted in good faith in protecting the interests of the body corporate and its members. The nature of the breach (misappropriation of monies held in trust) is material.</p>	<p>Yes.</p>