

15 March 2017

Honourable Chairman YI Carrim

The Standing Committee on Finance

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cc: Honourable Minister P Gordhan – Minister of Finance
Honourable Minister R Davies – Minister of DTI
Mr L Fuzile – Director-General, National Treasury
Mr Ismail Momoniat – Deputy Director-General: Tax & Financial Sector Policy, National Treasury
Adv Dube Tshidi – Executive Officer, FSB
Mr Jurgen Boyd – Deputy Executive Officer, FSB

LETTER TO THE STANDING COMMITTEE ON FINANCE (SCoF)

We, the undersigned organisations, are directly affected by current proposals from the Independent Regulatory Board for Auditors to introduce Mandatory Audit Firm Rotation (MAFR).

We are fully committed to responsible corporate citizenship; to strengthening audit independence; to quality corporate governance; to ensuring South Africa retains its position as the world leader in audit reporting standards and corporate governance.

We are also fully committed to transformation of the audit profession, to addressing market concentration and to working together with government to find ways of addressing these.

Notwithstanding the above: We firmly believe that **MAFR is not the correct instrument** to achieve greater audit independence, transformation of the profession, or market concentration, and that **IRBA is not the correct vehicle to drive such initiatives.**

Our concerns

We have two major concerns about MAFR as proposed by IRBA:

- Firstly, the proposal has implications far beyond the audit profession.
 - It would have a profound impact on the rights and interests of companies, investors and many stakeholders, and cuts across existing legislation such as the Companies Act, as well as conflicting with the King IV governance framework.
 - It also has the potential to cause serious harm to the economy, particularly given the costs involved in its implementation, and requires a much broader perspective than the one being applied by IRBA.
- Secondly, there are more effective ways of enhancing transformation of the audit profession, including the current transformation charter process that is underway, and the development of a new BBBEE code for the sector.

Given the implications for the country and the potential outcry if MAFR proceeds under IRBA's guidance, we feel compelled to point out that it would undermine business' confidence in government, concern foreign investors to the extent that their rights are being diluted, prompting them to withdraw capital, and possibly prompt corporates to move listings, which would have a significant impact on the JSE and foreign direct investment.

On top of this, there are clear limitations to the process that has already been embarked upon by IRBA:

- No evidence has been produced that shareholders, investors or other stakeholders in fact have real concerns about audit independence, which is supposedly the rationale for introducing MAFR.
- No evidence has been produced that the existing rules to entrench the independence of auditors have failed, nor is there evidence of significant deficiencies in the current levels of audit independence.
- No impact assessment has been conducted on the potential impact of MAFR and, as a result, there is no reliable or detailed analysis of how MAFR could improve audit quality.
- MAFR has already been rejected by most major markets, and has failed in most of the areas in which it has been introduced. At least 11 countries have scrapped it within a few years of introduction.
- The introduction of MAFR would come at a massive cost for the country. The EU, for example, estimates that the implementation of MAFR cost €16 billion, but the private sector believes it is at least double that. The cost in South Africa is conservatively estimated at R10 billion over 10 years. Effectively R1 billion a year.

In our view, the negative consequences of MAFR far outweigh any potential benefits. This has been clearly outlined to IRBA, but the regulator has either ignored or dismissed these concerns – causing great harm to the relationship between corporate South Africa and IRBA.

Proposal

We believe there are alternative routes that could be followed should there be a need to enforce greater audit independence, address market concentration or speed up transformation, and these should be explored.

These would include:

- The undertaking of independent research, including an impact assessment of the legal, regulatory and economic implications. We believe the Standing Committee on Company Law (SCCL) is the best vehicle for this process.
- A series of recommendations and options from the SCCL.
- Formulation of a White Paper.
- A public participation process through Parliament.

Alongside this, we would propose a proper process to enhance transformation in the auditing profession and to address market concentration. As the Department of Trade and Industry is the custodian of broad-based black economic empowerment codes it is, in our view, the appropriate vehicle to drive and monitor this process.

Conclusion

In summary, we propose the following roadmap:

- The process of assessing audit independence should take place within the framework of existing company law and best practice in terms of governance and the King Code, and should become the responsibility of the SCCL rather than IRBA.
- The transformation of the auditing profession – and within that, the question of market concentration – should be driven by the Department of Trade and Industry, and situated within a broad BBBEE process for the profession.

Once these two processes have been completed, IRBA could then be directed as to whether and how its own regulations for auditors need to be amended.

We trust our submission receives your favourable consideration.

Signatories

CFO Forum



Christine Ramon: Chairman – CFO Forum



Institute of Directors



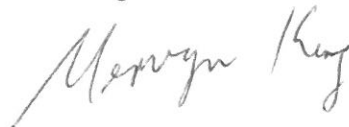
ASISA



Leon Campher: CEO – ASISA



King Committee



Audit Committee Forum



Barrie H Jack: Chairman – ACF