

Ref# 679204

24 July 2018

Mr. Jonathan Bravo
The International Organization of Securities Commissions (IOSCO)
Calle Oquendo 12
28006 Madrid
Spain

Email: consultation-04-2018@iosco.org

Dear Mr Bravo

SAICA SUBMISSION ON THE IOSCO CONSULTATION REPORT ON GOOD PRACTICES FOR AUDIT COMMITTEES IN SUPPORTING AUDIT QUALITY

The South African Institute of Chartered Accountants (SAICA) is the home of chartered accountants in South Africa – we currently have close to 44,000 members from various constituencies, including members in public practice ($\pm 30\%$), members in business ($\pm 58\%$), in the public sector ($\pm 5\%$), education ($\pm 2\%$) and other members ($\pm 5\%$). In meeting our objectives, our long-term professional interests are always in line with the public interest and responsible leadership. SAICA is currently the only professional accountancy organisation that has been accredited by the audit regulator in South Africa, the Independent Regulatory Board for Auditors (IRBA).

In response to your request for comments on the **Consultation Report on Good practices for Audit Committees in Supporting Audit Quality (Consultation Report)**, please find attached comments prepared by SAICA.

We thank you for the opportunity to provide comments on this document.

Please do not hesitate to contact us should you wish to discuss any of our comments. You are welcome to contact Willie Botha (willieb@saica.co.za) or Hayley Barker Hoogwerf (hayleyb@saica.co.za).

Yours sincerely

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Introduction and background from a South African perspective

1. SAICA's approach in responding to the Consultation Report was for the Assurance and Practices team as well the Legal and Compliance team to study and debate the recommended good practices outlined in the Consultation Report, in line with our understanding of how audit committees are currently functioning in a South African context, taking into account the requirements of the Companies Act, 71 of 2008 (Companies Act), the Johannesburg Stock Exchange (JSE) Listings Requirements as well as the governance principles and recommended practices contained in the King IV Report on Corporate Governance for South Africa, 2016 (King IV).
2. SAICA also consulted with members of its Assurance Guidance Committee and Legal Compliance Committee in obtaining their views and comments in finalising this comment letter.
3. In commenting on the recommended good practices contained in the Consultation Paper, we felt that it will be useful to provide the IOSCO with an overview of the current requirements and suggested practices in relation to audit committees operating in the South African environment.
4. The (Companies Act), which applies to all companies carrying on business within South Africa includes the following requirements in relation to audit committees:

Appointment of an audit committee

The shareholders are required to appoint an audit committee at every annual general meeting (AGM) for the following companies:

- A public company;
- A state owned company; or
- Other company where the company's Memorandum of Incorporation requires an audit committee¹.

Membership of an audit committee

Where a company is required to appoint an audit committee, the audit committee must consist of at least three members who meet the following criteria:

- every member must be a director of the company;
- a member may not be:
 - involved in the day-to-day management of the company's business or have been so involved at any time during the previous financial year;
 - a prescribed officer, or full-time employee, of the company or another related or inter-related company, or have been such an officer or employee at any time during the previous three financial years; or
 - a material supplier or customer of the company, such that a reasonable and informed third party would conclude in the circumstances that the integrity, impartiality or objectivity of that director is compromised by that relationship; and
 - related to any person who falls within any of the criteria set out in the previous points².

¹ Section 94(2), Companies Act

² Section 94(4), Companies Act

In accordance with the provisions of Regulation 42 of the Companies Regulations, 2011 (Companies Regulations) at least one-third of the members of a company's audit committee at any particular time must have academic qualifications, or experience, in economics, law, corporate governance, finance, accounting, commerce, industry, public affairs or human resource management.

Minimum duties of the audit committee

The audit committee has the duty to:

- nominate a registered auditor who, in the opinion of the audit committee, is independent of the company for appointment as auditor of the company;
- determine the fees to be paid to the auditor and the auditor's terms of engagement;
- ensure that the appointment made by the audit committee complies with the requirements of the Act and any other legislation relating to the appointment of auditors;
- determine the nature and extent of any non-audit services that the auditor may provide or that the auditor must not provide to the company or a related company;
- pre-approve any proposed agreement with the auditor for the provision of non-audit services to the company;
- prepare a report (which is to be included in the annual financial statements of the company):
 - describing how the audit committee carried out its functions;
 - stating whether the audit committee is satisfied with the auditor's independence; and
 - commenting in any way the committee considers appropriate on the financial statements, the accounting practices and the internal financial control of the company;
- receive and deal appropriately with concerns or complaints relating to:
 - the accounting practices and internal audit of the company;
 - the content or auditing of the company's financial statements;
 - the internal financial control of the company; or
 - any related matter;
- make submissions to the board on any matter concerning the company's accounting policies, financial control, records and reporting; and
- perform such other oversight functions as may be determined by the board³.

Neither the appointment nor the duties of an audit committee reduce the functions and duties of the Board of Directors of the company, except with respect to the appointment, fees and terms of engagement of the auditor⁴.

5. The JSE Listings Requirements include the following duties of the audit committee in addition to those contained in the Companies Act:
- Consider and satisfy itself of the appropriateness of the expertise and experience of the financial director;
 - Ensure that the issuer has established appropriate financial reporting procedures, and that those procedures are operating; and

³ Section 94(7), Companies Act

⁴ Section 94(10), Companies Act

- Request from the audit firm (and if necessary consult with the audit firm on) the information detailed in paragraph 22.15(h) in their assessment of the suitability for appointment of the audit firm and the designated individual audit partner⁵.

The audit committee is required to report to the shareholders, in its annual report, that it has executed the responsibilities set out in paragraph 3.84(g).

- The audit committee of an applicant issuer (i.e. a JSE listed entity or an entity applying for listing) must consider, when recommending an auditor for appointment or re-appointment at the annual general meeting of the entity (as well as prior to listing), that the entity may only appoint an audit firm that is accredited as such on the JSE list of Auditors and Accounting Specialists⁶;
 - When an entity receives notice from the JSE that their audit firm has been removed from the JSE list of Auditors and Accounting Specialists, or that their individual auditor has been included on the JSE list of Disqualified Individual Auditors, the audit firm and/or individual auditor, as may be applicable, must be replaced within 90 days of receiving such notification (there may be exceptions at the sole discretion of the JSE, as described in paragraph 3.87)⁷;
 - Subject to the provisions of the Companies Act, 2008 and the Memorandum of Incorporation of the applicant issuer and its subsidiaries, subsidiaries of applicant issuers are not required to be audited⁸.
6. King IV sets out the philosophy, principles, practices and outcomes which serve as the benchmark for corporate governance in South Africa⁹. With respect to the authority of King IV, it contains governance principles and recommended practices that form part of the entities' journey to good governance. King IV follows an approach of apply and explain. Entities, other than those listed on the Johannesburg Stock Exchange (JSE) are also encouraged to follow the governance principles and recommended practices as far as possible.
7. The application of the governance principles and recommended practices contained in King IV are generally voluntary. With respect to entities listed on the JSE, the JSE Listings Requirements have incorporated certain specific corporate governance practices from King IV with the intention of making their implementation mandatory¹⁰. The recommended practices incorporated in the JSE Listings Requirements applicable to audit committees are as follows:

All listed entities must in accordance with King IV appoint an audit committee. The composition of such committees must comply with the Companies Act (as applicable) and should be considered in accordance with the recommended practices in King IV on an apply and explain basis, provided that the audit committee must comprise of at least three members. A brief description of the committee mandate, the number of meetings held and other relevant information must be disclosed in the annual report¹¹.

⁵ JSE Listings Requirements, paragraph 3.84(g)

⁶ JSE Listings Requirements, paragraph 3.86

⁷ JSE Listings Requirements, paragraph 3.87

⁸ JSE Listings Requirements, paragraph 3.88

⁹ King IV, Introduction

¹⁰ Section 3.84, JSE Listings Requirements

¹¹ Section 3.84 (c), JSE Listings Requirements (own summary)

8. The recommended practices and principles contained in King IV applicable to audit committees are as follows:

Role of the audit committee

The role of the audit committee should be to provide independent oversight of, among others:

- The effectiveness of the organisation's assurance functions and services, with particular focus on combined assurance arrangements, including external assurance service providers, internal audit and the finance function; and
- The integrity of the annual financial statements and, to the extent delegated by the governing body, other external reports issued by the organisation¹².

The audit committee should oversee the management of financial and other risks that affect the integrity of external reports issued by the organisation¹³.

Membership of an audit committee

The members of the audit committee should, as a whole, have the necessary financial literacy, skills and experience to execute their duties effectively¹⁴.

All members of the audit committee should be independent, non-executive members of the governing body¹⁵.

The governing body should appoint an independent, non-executive member to chair the audit committee¹⁶.

Meetings of the audit committee

The audit committee should meet annually with the internal and external auditors respectively, without management being present, to facilitate an exchange of views and concerns that may not be appropriate for discussion in an open forum¹⁷.

Disclosures required in relation to the audit committee

The following should be disclosed in relation to each committee of the governing body:

- Its overall role and associated responsibilities and functions;
- Its composition, including each member's qualifications and experience;
- Any external advisers or invitees who regularly attend committee meetings;
- Key areas of focus during the reporting period;
- The number of meetings held during the reporting period and attendance at those meetings; and
- Whether the committee is satisfied that it has fulfilled its responsibilities in accordance with its terms of reference for the reporting period¹⁸.

¹² King IV, part 5.3, paragraph 51

¹³ King IV, part 5.3, paragraph 54

¹⁴ King IV, part 5.3, paragraph 55

¹⁵ King IV, part 5.3, paragraph 56

¹⁶ King IV, part 5.3, paragraph 57

¹⁷ King IV, part 5.3, paragraph 58

¹⁸ King IV, part 5.3, paragraph 50

In addition to required statutory disclosure and the disclosures recommended above, the following should also be disclosed in relation to the audit committee:

A statement as to whether the audit committee is satisfied that the external auditor is independent of the organisation. The statement should specifically address:

- The policy and controls that address the provision of non-audit services by the external auditor, and the nature and extent of such services rendered during the financial year;
 - The tenure of the external audit firm and, in the event of the firm having been involved in a merger or acquisition, including the tenure of the predecessor firm;
 - The rotation of the designated external audit partner; and
 - Significant changes in the management of the organisation during the external audit firm's tenure which may mitigate the attendant risk of familiarity between the external auditor and management¹⁹.
9. In reviewing the contents of the Consultation Report, no significant differences were noted between the recommended good practice and our understanding of how audit committees are currently functioning, taking into account the requirements of the Companies Act, the JSE Listings Requirements, as well as the governance principles and recommended practices contained in King IV.

Responses to specific questions asked

Questions relating to the role of audit committees and audit quality

1. Do you agree that audit committees can have an important role in supporting audit quality in the interests of market confidence in the quality of information in the financial reports of issuers (see Section 2.1)?

10. The auditor is ultimately responsible for audit quality. With this purpose in mind, the auditor performs an audit of financial statements in accordance with recognised and accepted auditing standards, such as the International Standards on Auditing (ISAs), while complying with relevant independence and other ethical requirements applicable to performing audits in a particular jurisdiction. Audit engagements are required to be performed within the overall context of a quality environment at audit firm level and at engagement level; i.e. the firm's system of quality control that is designed to ensure consistent high quality audit work, including that the audit reports issued by the firm or the audit partners are appropriate in the circumstances.
11. Such quality management requires the intimate involvement of the audit partner throughout the audit engagement and the diligent and effective application of the firm's quality control policies and procedures. Oversight by an external body such as the audit committee, who are cognisant of the best interests of the organisation and its stakeholders further enhances audit quality by bringing an essential element of objectivity to the evaluation of the organisation's (i.e. the audit entity's) assurance functions, including the external audit.
12. To this end, the audit committee should ask the right questions relating to the audit firm, the designated individual auditor and the related processes to satisfying themselves that the right level of audit quality is achieved and maintained. This includes questions around, among

¹⁹ King IV, part 5.3, paragraph 59

others, auditor independence; competency, including the availability of adequate resources with the appropriate training, skills and experience; the auditor's commitment to audit quality; as well as audit approach including significant risks identified and the auditor's response thereto.

13. We are therefore in agreement that the audit committee has an important role in supporting audit quality.

2. Do you have any comments on the background material on audit quality (see Sections 2.3 and 2.4)?

14. We are satisfied that the factors listed in the Consultation Report are valid and relevant.
15. Independence is not specifically mentioned in the Consultation Report as a factor that influences audit quality. Since audit firm and individual auditor independence is fundamental to audit quality, it is suggested that this be included as a separate factor.
16. Another factor that is, in our view fundamental to achieving audit quality and that should be included as a separate factor is the quality of the standards, including quality control standards, engagement standards and other relevant auditing pronouncements applied in performing the audit.

3. Do you have any comments on the proposed description of the roles and responsibilities of audit committees and auditors (see Sections 2.5 to 2.7)?

17. Taking into account the purpose and scope of the Consultation Report, which is to assist audit committees in considering ways in which they may be able to promote and support audit quality²⁰, we are satisfied with the description of the roles and responsibilities of the audit committees and auditors included in sections 2.5 to 2.7 of the Consultation Report.

Questions relating to proposed good practices (Chapter 3)

4. Do you have any comments on the proposed good practices for the features of audit committees that may facilitate a committee in being more effective in promoting and supporting audit quality (see Section 3.2)?
5. Do you agree with the good practices for audit committees outlined in Sections 3.3 to 3.9?
6. Do you have any additional suggestions on good practices to be adopted by audit committees (see Sections 3.3 to 3.9)?
7. Would you suggest any other changes to the proposed good practices outlined in this report? If so, in what manner (see Sections 3.3 to 3.9)?
8. In some cases a good practice is introduced with the words "The audit committee should take reasonable steps to ensure that" and in other case the words "The audit committee should consider the extent to which". Is the wording used for each good practice appropriate (see Sections 3.3 to 3.9)?

²⁰ Consultation Report, Executive Summary

18. In our response to specific questions asked, we have combined the response to questions four to eight, as follows:
19. With respect to the good practices included in Chapter 3 of the Consultation Report, the general consensus was that many of these practices are currently implemented in South Africa and therefore the issue of such guidance on good practices for audit committees would not result in significant changes to the manner in which audit committees currently operate.
20. The following comments on specific recommended good practices were noted.

Features of audit committees

21. From a South African point of view, the Companies Regulations require that at least one-third of the members of a company's audit committee at any particular time to have academic qualifications, or experience, in economics, law, corporate governance, finance, accounting, commerce, industry, public affairs or human resource management²¹.
22. Furthermore, King IV includes the principle that all members of an audit committee should:
- as a whole, have the necessary financial literacy, skills and experience to execute their duties effectively²²; and
 - be independent, non-executive members of the governing body²³.
23. We are therefore in agreement with the good practices contained in the Consultation Report with respect to the membership requirements of an audit committee.
24. A suggestion raised was that the Consultation Report should perhaps clarify that audit committee members should have unrestricted access to external consultants as deemed necessary and appropriate for the fulfilment of their position held on the audit committee.

Any audit tender or other selection process

25. Point 16 of the Consultation Report indicates that the auditors should be assessed against the criteria and selected having regard to audit quality. There was uncertainty around the reference to *the regard to audit quality* and how this is actually assessed and/or measured by the audit committee. It is not clear whether the items included in point 16 of the Consultation Report, namely skills, expertise, technical competence, and resource capacity are intended as audit quality indicators (AQIs) and if so, how does the audit committee actually go about assessing and/or measuring these AQIs in comparing and ultimately selecting an auditor for recommendation.
26. It is suggested that the Consultation Report clarify the intention behind including the items listed in point 16, namely skills, expertise, technical competence and resource capacity. It is further suggested that reference to guidance that is available in relation to the assessment and measurement of audit quality, such as available AQIs or resources where information on such indicators may be found be included in the Consultation Report.

²¹ Regulation 42, Companies Regulations

²² King IV, part 5.3, paragraph 55

²³ King IV, part 5.3, paragraph 56

27. We are aware of the following guidance in relation to understanding the concept of audit quality and the factors which impact it, that could be referred to in the Consultation Report:

Publication	Summary	Reference
A Framework for Audit Quality: Key Elements that Create an Environment for Audit Quality	Through this Framework, the International Auditing and Assurance Standards Board (IAASB) aims to raise awareness of the key elements of audit quality, encourage key stakeholders to challenge themselves to do more to increase audit quality in their particular environments, and facilitate greater dialogue between key stakeholders on the topic.	https://www.ifac.org/publications-resources/framework-audit-quality-key-elements-create-environment-audit-quality

28. The following is some prominent AQIs guidance that is available and that could be referred to in the Consultation Report:

Publication	Summary	Reference
The CAQ Approach to Audit Quality Indicators	<p>Released in April 2014, the CAQ Approach to Audit Quality Indicators represents a two-year effort by the Center for Audit Quality, with its member firms, to develop perspectives regarding which indicators of audit quality may be most relevant and how and to whom they should be communicated.</p> <p>The indicators represent four thematic elements of audit quality:</p> <ul style="list-style-type: none"> • firm leadership and tone at the top; • engagement team knowledge, experience, and workload; • monitoring; and • auditor reporting. <p>The paper sets forth in detail the set of potential indicators that are mostly focused at the engagement-level, an approach to communicating them that it is aimed at discussions between the engagement team and the audit committee, and the CAQ's plan to pilot test these indicators by member firms with select audit committees.</p>	https://www.the-caq.org/caq-approach-audit-quality-indicators?sfvrsn=2
Audit Quality Indicators: Journey and Path Ahead	<p>Released in January 2016, Audit Quality Indicators: The Journey and Path Ahead provides insights from a global series of roundtable discussions with audit committee members and other stakeholders on a potential set of audit quality indicators (AQIs).</p> <p>This outreach, together with the results from pilot testing</p>	https://www.the-caq.org/audit-quality-indicators-journey-and-path-ahead

Publication	Summary	Reference
	of the CAQ's Approach to Audit Quality Indicators, suggests a path forward on efforts to identify the most effective way to determine and assess audit quality.	
Concept Release on Audit Quality Indicators	<p>The PCAOB issued a Concept Release for comment on 1 July 2015 in which it proposed no fewer than 28 potential AQIs, categorised as follows:</p> <p>Audit professionals</p> <ul style="list-style-type: none"> • Availability of audit professionals • Competence of those performing the audit • Focus as indicated by audit hours, risk areas, etc. <p>Audit process</p> <ul style="list-style-type: none"> • An audit firm's tone at the top and leadership • Incentives (for example quality ratings, compensations, audit fees) • Compliance with independence requirements • Investment in infrastructure that support quality • Monitoring and remediation (including results on internal firm quality reviews and external inspection findings) <p>Audit results</p> <ul style="list-style-type: none"> • Financial statements, including restatements, financial reporting misconduct and other measures of financial reporting quality • Reporting of internal control weaknesses • Reporting of going concern issues • Communications between the auditors and the audit committee • Enforcement and litigation trends 	https://pcaobus.org/Rulemaking/Docket%20041/Release_2015_005.pdf
Information Paper: Overview of Audit Quality Indicators Initiatives Update to December 2015	<p>In this Information Paper, The Federation of European Accountants identified the following as the most popular suggestions for AQIs:</p> <ul style="list-style-type: none"> • Training hours per audit personnel • Internal engagement quality reviews • Number of audit staff per audit partner • Years of experience • External inspections • Partner workload • Industry expertise of audit personnel • Staff workload • Investment in development of new audit methodology and tools • Staff turnover • Independence • Staff satisfaction survey 	https://www.accountancyeurope.eu/wp-content/uploads/1607_Update_of_Overview_of_AQIs.pdf

Publication	Summary	Reference
	<ul style="list-style-type: none"> • External investigations • Technical resources 	

29. The placement of point 19 of the Consultation Paper was debated. This good practice makes reference to the *incumbent auditor* and *sufficiently recent partner rotation*. We agree that this is a good practice that has merit in being included in the Consultation Report but it is our view that this does not relate to the audit tender or other selection process and would therefore be better placed under the section entitled to *Independence and objectivity*.
30. The meaning of the term *over familiarity* included in point 19 of the Consultation Paper was also debated, with a question around what is considered to be *too familiar* and that would result in a threat to independence that cannot be mitigated to an acceptable level in the circumstances. Although the scope of the Consultation Report is not to prescribe requirements in relation to independence, it is suggested that this point be expanded to indicate that audit committees should be familiar with and consider the independence requirements of the relevant Code of Professional Conduct or Ethics for auditors in the jurisdiction and other independence requirements applicable to performing audits of financial statements in the jurisdiction, for example, those contained in law or regulation. This will ensure a focus on identifying those situations that may create a threat to independence that cannot be mitigated to an acceptable level by the application of safeguards.

Commitment to audit quality

31. Point 21 of the Consultation Report indicates that that audit committee should consider any indications that either the audit committee or management are aware of that the firm may not have a culture that sufficiently promotes audit quality. It is suggested that reference to other members of governing bodies of entities, such as non-executive directors also be included for completeness sake.

Resources devoted to the audit

32. Based on our reading of point 24 of the Consultation Report, it would appear that this point relates specifically to the tendering process and what needs to be demonstrated. It is therefore suggested that this point is better placed under the section entitled, *Any audit tender or other selection process*.

Audit strategy and scope

33. Point 32 of the Consultation Report recommends that the audit committee take reasonable steps to ensure that a continuing auditor has prepared a plan for the audit for discussion with the audit committee and that the audit committee should review such plan with regard to whether the auditor plans to address risks known to audit committee members. There is, however no guidance in relation to the timing of when such audit plan should be presented to the audit committee for review and consideration. It is suggested that the Consultation Report expand on this recommended good practice by indicating that the review and consideration of the audit plan by the audit committee should take place prior to the commencement of the audit.
34. During our consultations, a debate arose around the good practice included in point 33 of the Consultation Report and whether this recommended good practice perhaps results in the

audit committee overstepping into the territory of the external auditor. It was noted that these are very specific circumstances and the question around how far the Consultation Report should take this was debated. For example, if the Consultation Report recommends that the audit committee questions the auditor's decision around whether to test one or more of the significant systems supporting information in the financial report in accordance with the "once in every third audit" principle in accordance with ISA 315 (Revised), then why not also recommend that they question the auditors decision on, for example whether to follow a combined approach or fully substantive approach.

35. It is our suggestion that point 33 of the Consultation Report be replaced with a recommended good practice that the audit committee interrogate the audit plan with respect to significant classes of transactions, account balances and disclosures, and ask questions around the approach that the auditor has selected to follow.

Setting audit fees

36. In the introductory paragraphs included under section 3.5, *Setting Audit Fees*, the purpose and relevance of including the following sentence was questioned:

In any event, audit fees are usually a small proportion of costs, and reducing them does not generally have a significant impact on an issuer's profit.

37. Point 35 of the Consultation Report recommends that the audit committee evaluate the adequacy of audit fees in relation to the work required to support an audit opinion, without regard to fees that might be paid to the auditor for other services. The point was raised that, from an independence point of view, the audit committee should consider fees paid to the auditor for other services. Based on the current wording, this point may be misinterpreted. We suggest the following wording to clarify this recommended good practice:

Evaluate whether the audit fees charged by the auditor appear adequate in relation to the work required to support an audit opinion as a stand-alone engagement, without regard to fees that might be paid to the auditor for other services, as these should not be considered in the context of compensating for any shortfall in the audit fees.

Supporting the audit

38. With respect to point 40 of the Consultation Report, which recommends that the audit committee seeks explanations and advice supporting the accounting treatments chosen and, where appropriate, challenge the accounting estimates and treatments applied in the financial report, it is not clear who the audit committee seeks the explanations and advice from and who they are required to challenge on this. From the introductory paragraphs included under section 3.6, *Facilitating the Audit Process* as well as the fact that management are responsible for choosing and applying the accounting treatments and determining accounting estimates and treatments that are applied in the financial report, it can be deduced that this applies to management. However, based on title of the matter, *Supporting the audit*, it may be misinterpreted as implying that the audit committee should challenge the auditor on these matters. It is recommended that the Consultation Report clarify this.
39. To this point, it is also recommended that point 41 of the Consultation Report be clarified to indicate that any concerns or risks highlighted by the auditor are considered and addressed by management and, where appropriate, those charged with governance (in the context that these will be the parties who the auditor is expected to communicate with during the course of the audit in accordance with ISA 260 (Revised)).

Issuer management and staff

40. Point 42 of the Consultation Report recommends that the audit committee take reasonable steps to ensure that there is appropriate accountability and incentives for issuer management and staff to focus on the quality of financial reporting, timely reporting and facilitation of the audit process. We agree with the recommended good practice in relation to the audit committee ensuring that there is appropriate accountability but question the reason behind including the responsibility in relation to ensuring that there are appropriate incentives. It is our view that this does not form part of the good practices of an audit committee and is probably better placed within the ambit of a remuneration committee.

Independence and objectivity

41. Point 41 of the Consultation Report talks about situations when audit committees challenge complex accounting policy choices and estimates, and in line with our comment made in paragraph 38 and 39 of this comment letter, it is recommended that the Consultation Paper clarify who the audit committee is challenging in this regard. With the title of the section being *Independence and objectivity*, we assume that it relates to challenging the auditor but on the other hand management is responsible for accounting policy choices and estimates. Furthermore, this point makes reference to the audit committee seeking independent third-party advice rather than relying on the views of the auditor, which adds to the uncertainty. The various parties involved and the context within which each is considered by the audit committee should be clear.
42. In discussing this section, it was agreed that a good recommended practice was for the audit committee to have a policy regarding how to evaluate independence as included in point 46. The debate arose as to whether the Consultation Report should expand on this by providing a suggested outline for such a policy. It was agreed that the mere reference to having such a policy was sufficient without a suggested outline for the purposes of this Consultation Report.
43. A question around point 49 of the Consultation Report was raised as to why this independence requirement was singled out as requiring a specific policy as this is not the only matter that could impact on the auditor's independence. The recommended good practice should rather be that the audit committee establish an independence policy that incorporates matters that could impact on the auditor's independence for the audit committee to consider, taking cognisance of the relevant Code of Professional Conduct or Ethics for auditors in the jurisdiction and other independence requirements applicable to performing audits of financial statements in the jurisdiction. This would be consistent with the general understanding that the audit committee is required to have, as addressed in paragraph 30 of this comment letter.

Reporting to members/investors/ shareholders

44. From a South African point of view, King IV includes the following in relation to recommended disclosures that the audit committee should make in relation to auditor independence:

A statement as to whether the audit committee is satisfied that the external auditor is independent of the organisation. The statement should specifically address:

- The policy and controls that address the provision of non-audit services by the external auditor, and the nature and extent of such services rendered during the financial year;

- The tenure of the external audit firm and, in the event of the firm having been involved in a merger or acquisition, including the tenure of the predecessor firm;
- The rotation of the designated external audit partner; and
- Significant changes in the management of the organisation during the external audit firm's tenure which may mitigate the attendant risk of familiarity between the external auditor and management²⁴.

45. We are therefore in agreement with this good practice suggestion contained in the Consultation Report.

Addressing any relevant risk areas or areas of concern

46. Based on the practical experience of members that were consulted in informing this comment letter, it was noted that although the audit committee should take ultimate responsibility, some of the recommended good practices included in this section of the Consultation Report are actually performed by management and not the audit committee.

47. To this end, we suggest that the following points be amended as indicated:

- Point 56 – The audit committee ~~and ensures that~~ management informs the auditor in a timely manner about any relevant risks...
- Point 57 – The audit committee ~~and ensures that~~ management informs the auditor of the understanding of the business purpose of...
- Point 58 - The audit committee ~~and ensures that~~ management promptly informs the auditor of relevant correspondence or other communication...

Ensuring access to directors and audit committee

48. Included in point 66 of the Consultation Report is the recommendation that the audit committee meets with the auditor without management on a regular and frequent basis. The reference to a *regular and frequent basis* and the meaning thereof was debated.

49. From a South African point of view, King IV includes a recommended practice that the audit committee should meet annually with the internal and external auditors respectively, without management being present, to facilitate an exchange of views and concerns that may not be appropriate for discussion in an open forum²⁵.

50. It is common practice in South Africa for the audit committee to meet quarterly, but this would not necessarily include a separate meeting with the auditor; there may only be one such meeting on an annual basis. Would this be considered to be regular and frequent enough?

51. Furthermore, from a practical point of view, this recommendation may be difficult to implement in certain instances, in having to gather all members of the audit committee to meet with the auditor. Consideration should be given to expand the recommendation in terms of providing for meetings between the auditor and the audit committee or, alternatively, between the auditor and the chair of the audit committee for purposes of satisfying the intended practice of "regular and frequent" meetings.

²⁴ King IV, part 5.3, paragraph 59

²⁵ King IV, part 5.3, paragraph 58

The audit process

52. In reviewing the recommended good practice, it was noted that these points have been mentioned in other sections of the Consultation Report, as follows:

The audit process	Referred to other parts of the Consultation Report
69. The auditor demonstrates a sufficient understanding of the business, operations and risk areas relevant to the financial report, and has responded appropriately to assessed risks.	Resources devoted to the audit 24. The auditor demonstrates a sufficient understanding of the business, operations and risk areas relevant to the financial report, and plans to respond appropriately to assessed risks. In a tender process, sufficient access would normally be provided to management for a prospective auditor to obtain an understanding of the business, operations and risk areas.
70. The auditor appears to exhibit sufficient professional scepticism in challenging, rather than rationalising, estimates and accounting policy choices (e.g. complex or subjective asset valuations, including cases where the reported net assets exceed the market capitalisation of the issuer).	Addressing any relevant risk areas or areas of concern 60. The auditor demonstrates professional skepticism in considering judgement areas such as accounting estimates and accounting policies.

53. The rationale behind duplicating these points was debated. It would appear that these considerations are applicable to different stages during the course of the audit, but it is suggested that the Consultation Report clarify the need for, and distinction between these considerations at different stages or, alternatively, requiring a different context or perspective from the audit committee at different times.

Communication of issues

54. In the context of the comments provided in paragraphs 52 and 53 of this comment letter, above, the Consultation Report should also clarify the need for and distinction between the audit committee's considerations in points 72 and 73, compared to similar considerations relating to reports from the auditor addressed in point 59.

Other information

55. Point 74 of the Consultation Report recommends that information relevant to the audit quality in an audit firm's annual audit transparency report is reviewed. It is not clear who this information should be reviewed by. This is also not clear in Point 75 of the Consultation Report.
56. It is assumed that the Consultation Report is recommending that the audit committee should perform the review the information contained in Point 75 and 76 of the Consultation Report and if this is the case, we suggest the wording be amended as follows:

The audit committee should ~~consider the extent to which~~ review:

74. Information relevant to audit quality in an audit firm's annual audit transparency report ~~is reviewed~~.

75. Any other information on audit quality ~~is reviewed~~ (e.g. internal issuer staff observations or assessments of audit quality).

Findings from regulatory audit inspections and surveillances

57. The following amendments to the wording of points 77 and 78 are suggested to enhance the readability and understand ability of the Consultation Report:

~~The audit committee should consider the extent to which:~~

77. If a regulator selected the issuer's audit for review, the audit committee ~~has considered~~ should consider the review's scope and results when evaluating the auditor's performance and the quality of the audit.

78. The audit committee should review and consider any overall public aggregate thematic findings from a regulator's inspections or surveillances that are common across many audit engagements.

58. The rationale behind including point 79 of the Consultation Report as a recommended good practice was questioned. It was noted that this may be misinterpreted as meaning that it is common practice for auditors to downplay findings noted by regulators. The general consensus was that this recommend good practice is sufficiently covered in points 77 and 78 of the Consultation Report and it is therefore suggested that point 79 be removed.

Alternatively, the overall context for such a recommendation should be changed so as not to result in any unintended interpretation. For example, "If the auditor has provided certain explanations of the findings of an audit oversight regulator from the review of the audit files for the specific issuer, the audit committee should consider the rationale for such explanations, including requesting additional information from the auditor in this regard, as may be deemed necessary".

59. Another point that was debated in discussing this section was whether the recommended good practice relating to the review and consideration of the scope and results of the regulatory inspection applied to the firm inspection or the inspection performed on the designated individual audit engagement partner. It is suggested that the Consultation Report clarify that this recommended good practice is applicable to both the firm inspection and the inspection performed on the designated individual audit engagement partner.

9. It is proposed to provide good practices at principles level and not to include detailed procedures to support those principles. Do you agree with this approach (see Sections 3.3 to 3.9)?

60. From a South African point of view, the appointment, role and functions of audit committees are well established, in particular as it relates to certain categories of audited entities. It is possible that the introduction of detailed procedures on how audit committees should discharge part of their responsibilities will be met with some resistance. To this end, it is our

view that a document that contains recommended good practice at principles level will be better received by the market.

61. The inclusion of detailed procedures would also raise a concern that this may result in audit committees following a tick box approach in supporting audit quality and not applying their mind in how best to apply the recommended good practice principles.
62. We are in agreement with the approach to provide recommended good practices at principles level and not to include detailed procedures to support those principles.
63. In working through the detail contained in section 3.2 to 3.9 of the Consultation Report, we were generally satisfied with the level of detail included in each point. We have included specific comments in response to questions 4 to 8 above.

10. Given the differing governance structures for issuers in different jurisdictions, to what extent should any final good practices report deal with the roles of the governing board, audit committee and management in relation to financial reporting, systems and processes (see Section 3.6)?

64. It is our understanding that the scope of the Consultation Report is to assist audit committees in considering ways in which they may be able to promote and support audit quality²⁶.
65. Therefore, recommended good practices that address the roles of the governing board and management in relation to financial reporting, systems and processes are beyond the scope of the proposed report and it should not be expanded to include such.

11. What frameworks, practices, methodologies, or tools have audit committees found to be helpful in evaluating the following:

- a) Professional skepticism of auditors;
- b) An auditor's commitment to audit quality;
- c) Whether an audit firm's culture supports audit quality;
- d) Whether an audit firm has or makes available during an audit an appropriate level of resources with appropriate skills and expertise; and
- e) Whether audit quality has been compromised by reduced audit fees?

66. In terms of the time and resources we had available to do outreach and research for purposes of this comment letter, we were not able to sufficiently focus on any specific frameworks, methodologies or tools that audit committees currently use.
67. With respect to *practices*, the JSE listings requirements require the audit committee to request information from the audit firm for purposes of assessment of the suitability for appointment of the audit firm and the designated individual audit partner. The information that audit committees are required to request includes the following:

For the following for the latest inspection performed by the IRBA:

- The decision letter, findings report and the proposed remedial action plan to address the findings, on the audit firm;

²⁶ Consultation Report, Executive Summary

- The decision letter, findings report and the proposed remedial action plan to address the findings, on the individual auditor where the engagement file subject to the inspection was for that specific applicant issuer or one of its subsidiaries;
- The decision letter for all other engagement file reviews on both the individual auditor who will be the applicant issuers' designated individual auditor for the next audit and, if the audit firm remains unchanged, on the designated individual auditor for the past audit;
- Where necessary, an explanation of the above findings to ensure that there is an understanding of those findings in the appropriate context²⁷;
- a summary of the following information, which would have been communicated annually to the engagement partners and other appropriate individuals within the audit firm, including the firm's chief executive officer or, if appropriate, its managing board of partners in terms of paragraph 53 of ISQC 1 (and/or paragraph 54 in the case of a network):
 - a description of the monitoring procedures performed (Paragraph 53(a) of ISQC1);
 - the conclusions drawn from the monitoring procedures (Paragraph 53(b) of ISQC1);
 - where relevant, a description of systemic, repetitive or other significant deficiencies and of steps taken to resolve or amend those deficiencies (Paragraph 53(c) of ISQC1)²⁸; and
- the outcome and a summary of any legal or disciplinary proceedings concluded within the past 7 years, which were instituted in terms of any legislation or by any professional body of which the audit firm and/or designated individual auditor are a member or regulator to whom they are accountable, including where the matter is settled by consent order or payment of a fine²⁹.

Questions relating to other matters (Chapter 4)

12. Should the proposed report include a section mentioning the possibility of public reporting by audit committees on how they support audit quality? If so, should such reporting be described as "voluntary" or as a "good practice" for the majority of jurisdictions where there is no mandatory requirement? Should more detailed reporting criteria be provided in any final report (see Section 4.1)?

68. The inclusion of a section on public reporting by audit committees on how they support audit quality has the potential of driving positive behaviour in that audit committees think more deliberately about the role that they play in this regard.
69. From a practical point of view, one should also consider that the preparation of an audit committee report requires significant resources, particularly in drafting this report in the first year and there is the danger of generic, boilerplate reporting which adds little value.

²⁷ JSE Listings Requirements, paragraph 22.15(h)(i) (own summary)

²⁸ JSE Listings Requirements, paragraph 22.15(h)(ii) (own summary)

²⁹ JSE Listings Requirements, paragraph 22.15(h)(iii)

70. From a South African point of view, King IV recommends that the statement of the audit committee includes the audit committee's view on the quality of the external audit³⁰. In reaching this conclusion, it is likely that the recommended good practices as included in the Consultation Report were considered by the audit committee.
71. Furthermore, the Companies Act and the JSE Listings Requirements require that the annual financial statements of identified companies include an audit committee report which discloses, among other matters, how the audit committee carried out its functions and how it satisfied itself regarding the discharging of its responsibilities (refer to the background information provided in paragraphs 4 and 5 of this comment letter). Again, this would likely require consideration of the recommended good practices as included in the Consultation Report.
72. Since there are clear benefits to reporting on this nature, inclusion of such section will be beneficial in enhancing audit committees support of audit quality. The improved transparency about the role and functions of the audit committee would strengthen the trust in this important oversight mechanism. However, with the demand on resources and the fact that audit committee maturity may differ significantly between jurisdictions, it is suggested that reporting of this nature remain voluntary at present, thereby allowing different jurisdictions to determine the pace of this development in the context of their circumstances.

Other comments

13. Are there any other comments that you have on the proposed good practices report and the material that may be included in any final report?

73. Throughout the Consultation Report, the following terms are used:
- Auditor;
 - Auditor's engagement partner or Engagement partner;
 - Engagement quality control reviewer;
 - Audit team members; and
 - Audit firm.
74. In instances where reference is made to the *auditor*, there is uncertainty around the intended party to which this relates. In Chapter 2, this is not as a big concern as with Chapter 3, where there is uncertainty around whether the recommended practices relate to, for example the audit firm, the individual designated auditor or audit team members. It is therefore suggested that the term *auditor* be defined.
75. Included in the executive summary of the Consultation Report is a statement that the International Forum of Independent Audit Regulators (IFIAR) has reported that, according to audit regulators, auditors did not obtain reasonable assurance that financial reports were free of material misstatement in 40% of audits reviewed by audit regulators. We question the factual accuracy of this statement. Our reading and understanding of the 40% quoted in the IFIAR report is that 40% of the listed public interest entities audit engagements that were inspected had at least one finding. It is suggested that if this executive summary is intended to be included in the final report, this statement be reconsidered.

³⁰ King IV, part 5.3, paragraph 59 (c)