LETTER FOR AUDITORS TO SEND TO
CLIENTS OUTLINING THE
REQUIREMENTS OF SECTION 45 OF
THE AUDITING PROFESSION ACT –
THE DUTY TO REPORT ON
REPORTABLE IRREGULARITIES

Introduction
The enactment of the Auditing Profession Act (Act 26 of 2005), has placed a requirement on auditors relating to the reporting of reportable irregularities.

The Auditing Profession Act does not explicitly require audit practitioners to inform their clients of the legislative requirements associated with reportable irregularities, however it is believed to be good practice. There are numerous methods in which a practitioner could communicate on this topic with their client, a letter being one of them. The purpose of this circular is to provide guidance to auditors regarding the form and content of the letter that could be sent to clients, informing them of the legislative requirements associated with reportable irregularities. Further guidance relating to reportable irregularities can be found in Reportable Irregularities: A Guide for Registered Auditors, issued by the Independent Regulatory Board for Auditors.

Appendix A presents a draft letter for auditors to send to clients outlining the requirements of the Auditing Profession Act and more specifically the requirements of section 45, which deals with the duty to report on irregularities.

The applicable sections of the Auditing Profession Act are reproduced here for information purposes.
“Definitions

‘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;”

“45. Duty to report on irregularities

(1)(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.

(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 that 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;

(b) afford the members of the management board of the entity an opportunity to make representations in respect of the report; and

(c) send another report to the Regulatory Board, 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).

(4) The Regulatory Board must as soon as possible after receipt of a report containing a statement referred to in paragraph (b)(i)(cc) of subsection (3), notify any appropriate regulator in writing of the details of the reportable irregularity to which the report relates and provide it with a copy of the report.

(5) 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.

(6) Where any entity is sequestrated or liquidated, whether provisionally or finally, and a registered auditor referred to in section 44(l)(a) at the time of the sequestration or liquidation –

(a) has sent or is about to send a report referred to in subsection (1) or (3), the report must also be submitted to a 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.”

“52. Reportable irregularities and false statements in connection with audits

(1) A registered auditor who –

(a) fails to report a reportable irregularity in accordance with section 45; or

(b) 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.

(2) 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).

(3) 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."

Johannesburg            IS Sehoole
April 2007                                                               Executive President
Appendix A

A draft letter for practitioners to send to clients outlining the requirements of the Auditing Profession Act, and more specifically, the requirements of section 45 – the duty to report on reportable irregularities.

[Firm Letterhead]

Dear …………..

[Add introduction as necessary]

Reporting to the Independent Regulatory Board for Auditors, in terms of section 45 of the Auditing Profession Act, 2005

You may be aware from press and other reports that new legislation regulating auditors has been enacted during 2006.

I have a statutory obligation to report certain matters to the Independent Regulatory Board for Auditors (IRBA). I am writing to you to provide a brief overview of the new reporting obligations imposed by the Auditing Profession Act.

The new legislation brings into existence a new regulator in the form of the IRBA which supersedes the Public Accountants’ and Auditors’ Board (PAAB).

Section 45 of the Auditing Profession Act places a legal requirement on the auditor to report to the IRBA, without delay, details of any reportable irregularity which comes to my attention, and which I am satisfied or have reason to believe has taken place or is taking place in respect of [entity name].

The Auditing Profession Act defines a reportable irregularity as “any unlawful act or omission committed by any person responsible for the management of an entity, which:
• 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
• is fraudulent or amounts to theft; or
• 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.”

Matters which come to my attention and meet the definition above are clearly of a serious nature. In addition to reporting such matters to you and to those charged with the governance of [entity name], I am obliged to report such matters to the IRBA.

Accordingly, the South African Institute of Chartered Accountants, of which I am a member, has advised its members who practice as auditors to write to their audit clients informing them of the requirements of the section that deals with reportable irregularities and of the implications of this section.

What must the auditor do?

1. In terms of the legislation, if an auditor of an entity is satisfied, or has reason to believe that a reportable irregularity has taken place or is taking place, he or she must, without delay, send a written report to the IRBA.  

2. The report must give particulars of the alleged irregularity.

3. The auditor must notify the members of the management board of the entity in writing within three (3) days of sending the report.

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1 In order to satisfy him/herself that a reportable irregularity has taken place or is taking place, the auditor may carry out such investigations that the auditor considers necessary. 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 initial report on the potential reportable irregularity.
4. The auditor must take all reasonable measures to discuss the report with the members of the management board of the entity.

5. The auditor must afford the members of the management board an opportunity to make representations in respect of the report. The auditor must send another report to the IRBA within 30 days of the initial report to the IRBA, stating in his or her opinion on whether or not a reportable irregularity has taken place or is taking place. This report should also deal with whether adequate steps have been taken for the prevention or recovery of any loss.

6. The auditor may carry out such investigations he or she may consider necessary to comply with the above requirements.

7. The auditor must modify the audit report where the reporting process to the IRBA is incomplete; or where a reportable irregularity did exist, even if it is no longer taking place; or where the reportable irregularity is continuing.

8. It is important to note that the procedure described above must be carried out regardless of how the auditor came to know of the irregularity.

What must the IRBA do?

Where the irregularity is continuing the IRBA has a responsibility to report to an appropriate regulator (which includes any government agency), e.g. the South African Revenue Services, the South African Police Services or the Financial Services Board.

Possible penalties

I need to draw your attention to the fact that if the auditor fails to report a reportable irregularity, he or she may be guilty of an offence and may be liable to a fine of up to R10 million or imprisonment for a term not exceeding ten years, or both a fine and imprisonment.
Summary

As mentioned previously, the auditor’s responsibility with regard to reportable irregularities are well defined and can have serious consequences on the auditor if not followed appropriately.

While I am certain that you are committed to ensuring that such reportable irregularities do not exist, or that if they do arise they are dealt with appropriately according to applicable legal requirements, you may wish to further discuss the contents of this letter or the reporting obligations with me.

[Add other comments as appropriate e.g. comment regarding quality of service.]

Yours sincerely
Registered Auditor
Chartered Accountant (SA)