The Regulation of the Accountancy Profession
in South Africa

Draft Concept Paper

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1. The Need for Regulation of the Profession

The collapse of large financial institutions in several countries as well as the failure of Enron, Worldcom and Leisurenet have tarnished the reputation of the accountancy profession in South Africa and in the rest of the world. In the wake of these events, the business community and governments in many countries have initiated a drive to increase the regulation of the profession.

The regulation of the profession ensures that accountancy professionals follow the highest standards and ethical behaviour. This has greatly contributed to uplifting the image of the profession. By 2013, the profession and its mother body, the International Federation of Accountants (IFAC), have managed to notably improve the international image of the accountancy profession again. Stringent regulations and high standards set by professional accountancy bodies and IFAC have helped the global accountancy profession over the past few challenging years that were marked by recessions and a loss of trust in financial markets, companies and professionals working in the financial field.

The accountancy profession plays an important role in the South African economy through the provision of key services to individuals and businesses of all sizes, from large corporates to small- and medium-sized businesses (SMEs). The latter in particular are considered the engines of growth and job creation. The services that accountancy professionals render to their respective clients have much more far-reaching effects than just between the two parties that are directly involved. The services also influence the decisions of investors and creditors, to name just a few. Compliance with ethical, technical and professional standards is therefore even more important.

Service markets in general – and the market for accountancy services in particular – have some specific features that need to be taken into account when it comes to the regulation of the profession. Contrary to product markets, a service cannot be evaluated prior to the purchase. Clients can only see and evaluate the quality of the service after purchasing it, whereas products can generally be evaluated and compared much more easily before a purchase decision is made. The market for the services that the accountancy profession offers is thus characterised by both externalities and information asymmetries.

- **Externalities** exist because there are significant benefits and/or costs that accrue to third parties (parties that are not part of the contracting parties) when accountancy services are provided. In such a context, appropriate regulation can ensure that the costs and/or benefits to third parties are considered in the decision what services are to be produced and in which quality. An example for positive externalities of accountancy services are financial statements. These have a wider use and benefit that includes current and potential future investors who receive the information that they require to make informed (dis)investment decisions based on these financial statements.

- **Information asymmetries** frequently occur between clients and accountancy professionals. It is most difficult (if not impossible in some instances) for clients to judge the professional expertise of an accountancy professional and the quality of the services in advance, i.e. before the services are rendered. Setting clear and uniform
qualification requirements and professional standards (e.g. in terms of ethical behaviour) that need to be met by every accountant help assure clients and businesses of a sufficiently high level of expertise and quality when acquiring the services of a professional accountant. Regulation can thus instil trust in the members of the profession and ensure that they keep up good standards and abide by ethical principles.

Similar to the regulation of other professions, the regulation of the accountancy profession is a specific response to the need that the members of the profession meet certain standards and provide an appropriate and consistent quality of their services. To warrant high and consistent quality, strict compliance with ethical, technical and professional standards is indispensable. Since the accounting profession provides an important public service, it is vital that the profession at large and each of its members serves, acts and operates in the public interest.

The past few years have illustrated the importance of standards and consistently high quality in re-gaining trust in the services offered by accountancy professionals. Clients and other stakeholders need to be assured – more than ever – that the services rendered by accountancy professionals are of a consistently high standard and are in line with best practices and ethical principles. After all, the sustainability and the reputation of the accountancy profession crucially depend on:

- the quality of the services that its members provide;
- the profession’s ability to respond to the demands of the economy and society in a quick, effective and efficient way.

Appropriate regulation of the profession is a key instrument to achieve these goals. This concept paper sets out the position of the Forum of Accounting Bodies (FAB) towards the regulation of the accountancy profession in South Africa and suggests a way forward to devise and implement an efficient and effective form of regulation of the profession.

2. Introduction to FAB

The Forum of Accounting Bodies (FAB) of South Africa was formed in 2010. FAB is based on a concept similar to the Consultative Committee of Accounting Bodies (CCAB)¹ in the UK and has the following broad objectives:

- To represent the South African Accountancy Profession in discussion and liaison.
- To act in concert and to develop joint representation to government and governmental bodies on legislation and the public matters which affect the business or professional interests of their members, and similarly to other public institutions and bodies.
- To identify potential matters of common interest to the Accountancy Profession.

¹ See http://www.ccab.org.uk/
The following four Professional Accounting Bodies, who are full members of the International Federation of Accountants (IFAC), are the founder members of FAB:

- Association of Chartered Certified Accountants (ACCA)
- Chartered Institute of Management Accountants (CIMA)
- South African Institute of Chartered Accountants (SAICA)
- South African Institute of Professional Accountants (SAIPA)

Two other professional bodies have been co-opted as members to FAB:

- Chartered Secretaries Southern Africa (CSSA)
- Institute of Internal Auditors (IIA)

The Chair of the Forum rotates and is currently held by Mr Shahied Daniels of SAIPA. The Forum of Accounting Bodies believes that its formation represents an important step in creating a common voice and platform for the Accountancy Profession in South Africa, which has an important function to fulfil in the South African economy.

3. The Current Regulation of the Profession

The auditing leg of the profession is regulated though a single, comprehensive piece of legislation, namely the Auditing Profession Act, No. 26 of 2005. The Act addresses the education, training and professional development of registered auditors, sets out the rules and requirement for the accreditation of professional bodies and provides for the registration of auditors. The Act also lays out clear duties, conduct by and the liability and accountability of registered auditors.

The Auditing Profession Act repealed the PAA Act, No. 80 of 1991. As a consequence, the Public Accountants’ and Auditors’ Board (PAAB) was replaced by the Independent Regulatory Board of Auditors (IRBA). The Auditing Profession Act thereby separated the regulatory framework of the auditing part of the profession from that of the accounting part of the profession. Up to this day, the non-auditing part of the profession remains less regulated. The current regulation of this part of the profession tends to be fragmented and focuses on specific aspects (e.g. SARS obviously focuses on the tax perspective).

The Forum of Accounting Bodies is of the opinion that the non-auditing part of the profession should be regulated too, similar to the auditing part of the profession. This is even more important in view of the key role and function that accountancy professionals assume in the economy. It would be desirable to obtain a consolidation of the fragmented legislation, which provides a clear and comprehensive regulatory framework for the accountancy profession.

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4. Effective Regulation in the Public Interest

Accountancy professionals offer their services all over the country to individuals and companies of different sizes across all sectors. The importance of their services and the far-reaching effects, together with the fact that their services are characterised by externalities and information asymmetries, constitute an inevitable need for effective regulation of the profession.

In designing and implementing regulation for the accountancy profession, it is important to carefully consider the nature, the characteristics and the operation of the market for these services. Otherwise, there is a risk that the regulation does not address the issues in a corrective way and that it does not achieve its purpose or at least not to its full extent. In the worst scenario, ill-devised regulation can even cause more costs than benefits to the economy, to society and to the profession.

Through their knowledge of the profession, accountancy bodies can contribute to the creation of effective and efficient regulation for the profession. Professional bodies therefore have an obligation to share their knowledge of the profession and the markets in which they operate with the regulator. Acting in the public interest, professional bodies should communicate and collaborate with the government to assist in the design and implementation of high-quality professional regulation that benefits not only the profession, but most importantly the economy at large.

There are various options how and by whom the profession can be regulated. These range from a complete self-regulation through professional bodies to a complete external regulation:

- **Self-regulation** has three major advantages. Firstly, professional bodies are close to their members and have a profound knowledge of the market in which they operate. This gives them a good sense of how regulations will affect their members’ behaviour. Secondly, professional bodies have better and easier access to the relevant information and can also draw upon the skills and experience of their members to regulate the profession and set appropriate standards. And lastly, professional bodies are generally able to respond and act more quickly than a government regulator when the relevant circumstances change.

- **External regulation** means that the profession is regulated by the government, either through a government agency or through an independent agency that was created and delegated regulatory powers by the government. The major advantage attributed to external regulation is the regulator’s independence of the accounting profession and of any accountancy organisations.

International examples show that self-regulation and external regulation can be successfully combined in different ways to create an efficient and effective mix of regulation. Regulatory responsibilities can, for instance, be shared such that the government or some independent agency is responsible for some aspects of regulation, while accountancy bodies are responsible for the other aspects of regulation (particularly for those in which they have more expertise than the government, e.g. education requirements for accountancy professionals).
The regulation of the accountancy profession should at least cover the following areas:

- Requirements for entry and licensing (including education and CPD\(^3\) requirements);
- Setting the basic code of conduct for accountancy professionals;
- Monitoring of the performance and behaviour of accountancy professionals;
- Standard setting (including ethical standards);
- Disciplinary rules and procedures for members of the profession who fail to meet the requirements or standards.

Accountancy bodies have much expertise in these areas and can effectively monitor the compliance of their members acting in their professional capacity. They are also usually more familiar with their members, their concerns and the issues affecting the industry. Accountancy bodies moreover tend to recognise emerging trends and issues in the profession at an early stage and can act in a quick and proactive manner. Their in-depth understanding of what is happening within the profession puts accountancy bodies in a prime position to assess which areas require some form of regulation, what the potential impact of such regulations will be and how to design regulations and standards such that they address the issues in an effective and efficient way and at the lowest possible cost.

The credibility and trust in the profession can further be enhanced if the government or an independent body/agency (with regulatory powers delegated by the government) exercises oversight activities over the self-regulation by the professional bodies and if the latter have to report to this agency in the discharge of their accountability. With a delegation of regulatory powers from government, FAB as a consultative body could assume these oversight responsibilities over the individual accountancy bodies and ensure that the self-regulation of the profession by these accountancy bodies is carried out in an effective and efficient way. A charter as well as clear rules and powers over the individual bodies would warrant FAB’s successful oversight activities to the benefit of the profession and the country.

The regulation is shared in a similar manner in the United Kingdom. The self-regulation of the profession is such that professional accountancy bodies have the primary direct regulatory responsibility to supervise their members acting in their professional capacity. The UK government is responsible for the legislative/statutory part of the regulatory framework. The Financial Reporting Council (FRC) is the UK’s independent regulator. It acted as an advisor to the government on required legislative changes. After the implementation of the new regulatory framework, the government delegated certain of these statutory powers to the FRC, but is still responsible through these powers and thereby has an ongoing responsibly for the effectiveness of the system. The Professional Oversight Board (POB), which is part of the FRC, is responsible to oversee the regulation of the accountancy and actuarial professions by their professional bodies. In doing so, the FRC ensures that the self-regulation of the accountancy profession is effective.\(^4\)

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\(^3\) Continuous Professional Development

By combining self-regulation and external regulation, it is thus possible to realise the advantages of both regulatory approaches. While self-regulation surely has a number of advantages and is traditionally favoured by most professions, FAB recognises that external regulation has benefits too. Sharing regulatory responsibilities with the government in the form of self-regulation combined with public oversight and accountability, such as it is done in the United Kingdom, is an efficient and effective way of regulating the accountancy profession. If every person working or acting as an accountant is obliged by law to be registered with one of the accountancy bodies in the country, self-regulation combined with public oversight and accountability is an optimal form of regulation that warrants an efficient and effective regulation of the accountancy profession.

5. Proposition for the Regulation of the Profession

The Forum of Accounting Bodies was founded as a representation of and platform for the Accountancy Profession in South Africa to give it a common voice. FAB shares IFAC’s view that professional accountancy organisations must work with the government to ensure that regulation is effective, efficient and in the public interest. Irrespective of how the regulatory responsibilities are shared, a collaborative and mutually respectful relationship between the government and the accountancy bodies promises the best outcome. FAB therefore endeavours to engage with the relevant government departments and stakeholders to discuss the options on how to drive the regulation of the profession forward and the best procedure to follow to regulate the accounting part of the profession.

For the reasons set out in this Concept Paper, FAB is convinced that the self-regulation of the profession combined with an oversight mechanism warrants the best outcome for the profession and for the economy at the lowest possible cost. It therefore proposes that:

1) Government recognises the Forum of Accounting Bodies (FAB) and authorises it as a consultative body that represents the professional accountancy bodies and the accountancy profession in South Africa.

2) FAB is delegated the responsibilities outlined in Section 4 of this Concept Paper and that this consultative body will be in charge of exercising oversight over the self-regulation of the individual professional bodies in the country.

The Forum strives to cooperate and work with the government and all the relevant stakeholders from the beginning of the process on to ensure an optimal and widely accepted regulatory framework of the profession. FAB firmly believes that ongoing dialogue is an essential condition for regulation and any regulatory system to be developed that is efficient, effective and beneficial to both the South African economy and the profession.

An analogous concept applies to attorneys. The Law Society of South Africa states that “In terms of the Attorneys Act, 1979 attorneys must register with the provincial law society where they practice, so attorneys are members of the four provincial law societies.” http://www.lssa.org.za/?q=con,67,History

FAB welcomes any comments and suggestions regarding the regulation of the profession, the content thereof and the process.

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