

This requirement seems to be in conflict with section 440X(3) and will limit the membership of the Panel to previous Panel members.

*We suggest that the Panel should from time to time be renewed with appropriately qualified persons that were not previous members of either the GAAP Monitoring Panel or the Panel.*

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### **Part 3: General Comments**

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#### **1. International Developments on Differentiating Accounting Standards**

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- **IFAC**

The International Federation of Accountants (IFAC), the worldwide organisation for the accountancy profession with a current membership of over 160 professional accountancy bodies in 120 countries, representing more than 2.5 million accountants in public practice, education, government service, industry and commerce, in June 2004 issued a Discussion Paper in which they describe the need to provide for a different approach for SME's in relation to the establishment of accounting standards. The Discussion Paper, in motivating for the development of differentiated accounting standards for SME's, uses words such as "difficulties", "excessive costs", "unnecessarily demanding" and "resulting information is not relevant for or used by the users of financial statements of SMEs".

According to the Discussion Paper (IFAC, 2004):

"In most countries, many or even all entities have a statutory (ie legal) obligation to prepare financial statements that conform to a required set of accounting principles that are generally accepted in that country (national GAAP). Those statutory financial statements are normally filed with a government agency and thus are available to creditors, suppliers, employees, government and others. The great majority of those entities are small or medium-sized entities (SMEs)—no matter how one might define 'small' or 'medium-sized'.

In some smaller or emerging economy countries, IFRSs are used as national GAAP for all or many unlisted entities. Thus, SMEs are required to follow all of the requirements of IFRSs. Not all of those SMEs have cited difficulties in applying IFRSs. However, there are many cases in which particular standards are departed from (sometimes with and sometimes without disclosure), and IFRSs are applied without rigorous enforcement or quality control. Also, SMEs often cite difficulties or excessive costs in applying IFRSs.

Some commentators argue that identical standards ought to be applicable to all financial statements that purport to give a fair presentation. Others advocate simplified or different standards for small or non-public entities, reasoning that some IFRSs are unnecessarily demanding for non-public entities, and some of the resulting information is not relevant for or used by the users of financial statements of SMEs. Those who hold the latter view have called for exemptions and modifications of IFRSs for small or non-public entities or, alternatively, for two separate sets of accounting standards, with one specific to small or non-public entities."

- **AICPA**

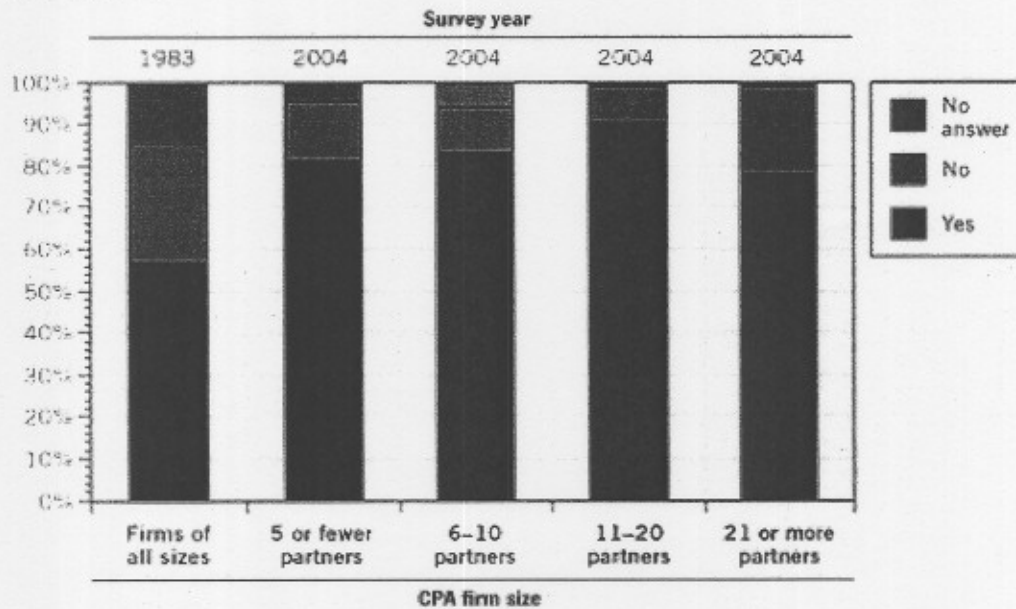
The American Institute of Certified Public Accountants recently issued a special report (AICPA, 2005) on whether GAAP should be developed for Private Companies. The Article reported that:

"Drawing on its research, the task force concluded that a customized version of GAAP should be developed based on concepts and accounting that better meets the needs of private company financial reporting constituents, whose information requirements are different in certain instances than those of groups using public company reports. This can be accomplished, the report said, by fundamentally changing the current GAAP standard-setting process in a manner to be determined by further discussion.

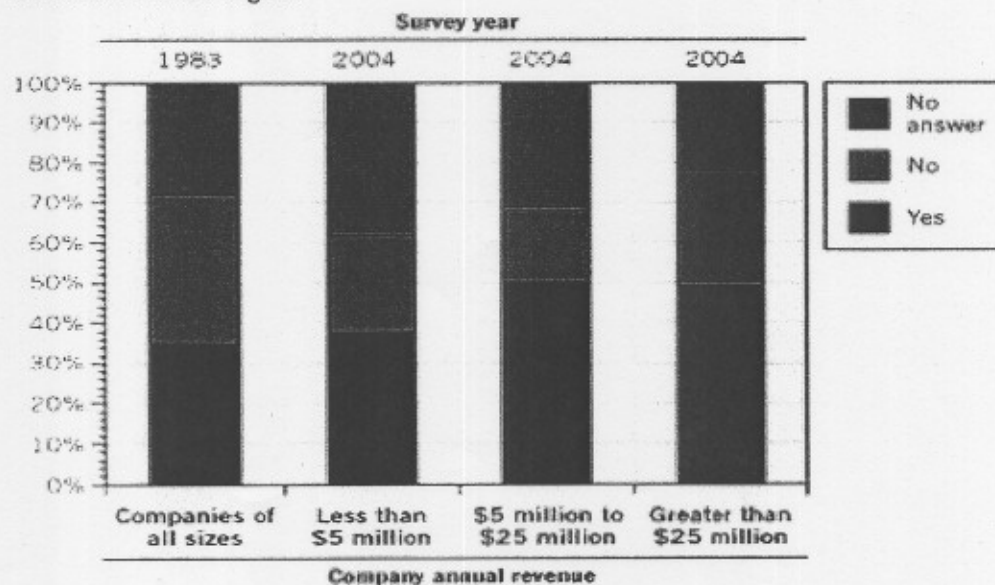
The report also noted that although private company financial statement preparers sometimes use GAAP exceptions and other bases of accounting, such usage is not always appropriate—even when there is no current alternative—because it erodes GAAP's consistency while failing to truly satisfy private company financial report users."

The special report also gave the following interesting responses from Owners and Managers, Practitioners and External Stakeholders on the question "Would it be useful if the underlying accounting in GAAP reporting were different, in certain instances, for public vs. non-public companies? These statistics reveals an overwhelming support for a differentiated approach.

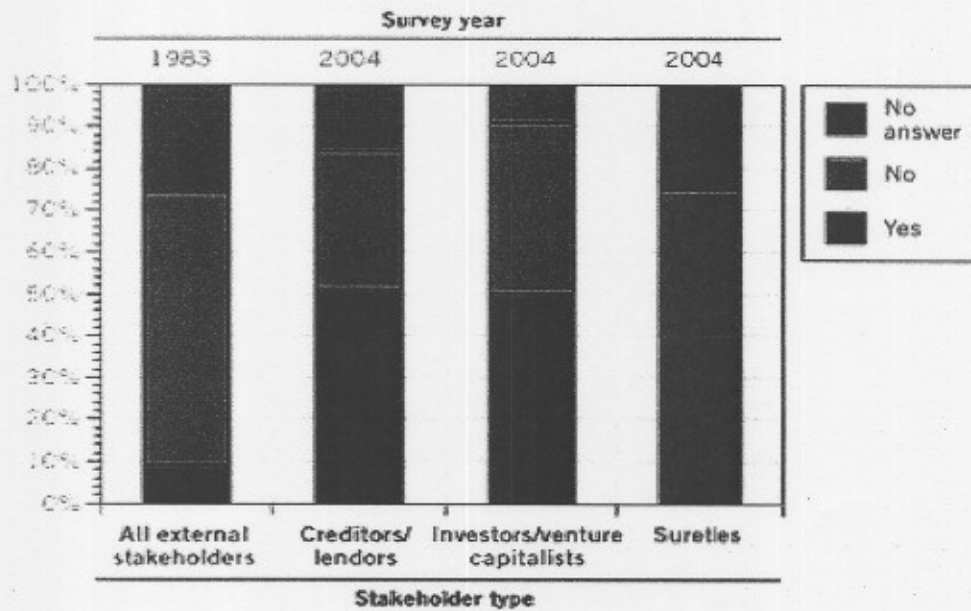
### Practitioners



### Owners and Managers



## External Stakeholders



- **South Africa**

The South African Institute of Professional Accountants has been part of the South African process to investigate and comment on appropriate accounting standards for private companies since 2002. We were members of the South African Institute of Chartered Accountants (SAICA) committee that gave commentary on the original Draft Financial Reporting Bill. We are also a member of the Eastern Central and Southern African Federation of Accountants (ECSAFA) standard-setting committee that established a guide on the implementation of private company accounting standards for ECSAFA member bodies.

We fully support the process of establishing a separate set of accounting standards for private companies and other legal entities that are used for business purposes.

It is therefore evident from the IFAC discussion paper, the AICPA special report and the South African process that a clear need exist for separate accounting standards for private or limited interest companies.



We applaud the Department of Trade and Industry for giving effect to this need. We fully support the process of establishing a separate set of accounting standards for private companies and other legal entities that are used for business purposes. .

The Memorandum to the Bill paragraph 4.8 reveals a deep understanding for the need to differentiate between companies. The Memorandum appropriately applies the "Thinking small first" principle:

"Since the standard to be imposed is primarily for the benefit of investors, and since it is an onerous standard, it is necessary to make provision for closely held companies that do not offer their shares to the public. The amendments thus propose a category of company referred to as "limited interest companies", which will be allowed to comply with a less onerous standard than the one imposed on other companies (viz. "public interest companies"). To qualify as a limited interest company, a company's articles will have to restrict the transferability of its shares and preclude any offer of its shares to the public."

We believe that this statement is key to the comprehensive review of South Africa's Companies Act, currently being conducted by the Department of Trade and Industry. Consistently applying the principles espoused within paragraph 4.8 will aid in the reduction of compliance cost and the increase in economic growth in the closely-held company environment.

## **2. Audit exemption**

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Since South Africa is now reviewing its Companies Act, an important decision will have to be made on whether the audit of companies will remain a mandatory requirement for all types of companies, irrespective of whether they are closely-held or widely-held.

Historically the primary reason for the statutory audit has been the separation of ownership from management.

It is the auditors function to determine whether the financial statements of a company fairly reflect the company's position in order to firstly assist the company in detecting errors and secondly to provide shareholders with reliable information to enable them to evaluate the conduct of managers.

Forcing the audit on companies or other entities where the separation of ownership and management does not apply or requiring the appointment of an auditor where management, shareholders or other stakeholders can obtain relevant and reliable information from other sources would be both inappropriate and impractical, and not inline with the principle espoused in paragraph 4.8 of the Memorandum to the Corporate Law Amendment Bill, B6-2006. Retaining the audit exempt will also place South Africa out of step with many other international jurisdictions.

- **The UK perspective**

Since 1993 audit exemption has been part of UK company law. The initial threshold was determined at a very low level but has in recent times been increased significantly to make the voluntary audit regime applicable to 80% of all UK companies that have to file accounts. 891 000 of 1 115 000 companies in the UK can make use of the audit exemption regime.

This increase was necessitated by recent developments in the European Union to increase the audit exempt threshold as well as the waning influence of UK company law.

In the UK a company would be audit exempt if it fell below two of three criteria for two consecutive years. The thresholds were recently increased and are currently set at £5.6 million turn over; £2.8 million balance sheet total; 50 employees.

- **International perspective**

Thresholds are not used by New Zealand, Canada or the United States in determining when an audit is required.

All owner/managed or private companies are exempt from the audit requirement in these jurisdictions.

Shareholders can by unanimous resolution decide not to appoint an auditor or minority shareholders can be protected by allowing a minimum number of shareholders to demand an audit.

### **3. Legislative Recognition for Professional Accountants**

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The role of the professional accountant becomes increasingly important in that government has made clear its intention to give legal backing to financial reporting standards.

If financial reporting standards receive legal backing it is submitted that companies will require the assistance of properly trained and professional persons to prepare the financial reports on their behalf. Professional accountants can fulfil this role in the new company dispensation.

However in South Africa persons that prepare financial statements for own account for business entities, including companies, are not required by law to be members of a professional accountancy body such as SAIPA, ACCA, CIMA and SAICA. This means that they are not subject to the same code of conduct as a professional accountant, yet they may advertise their services as accountants.

We believe that legislative recognition should only be given to appropriately qualified persons. This recognition can be given in the form of a Professional Accountants Act, which should be administered by the Department of Trade and Industry.

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**Part 4: Summary of proposals: Specific Comments**

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**Part 5: Amendment of section 28 of Act 61 of 1973**

*We suggest that the Bill should explain clearly what is meant by this phrase "prescribed manner".*

**Part 7: Amendment of section 38 of Act 61 of 1973**

*We therefore suggest that an amendment be considered that will:*

- *require fair value in terms of the amended section 38 but that will,*
- *not require fair value as part of the presentation of financial statements i.e. schedule 4.*

**Part 13: Amendment of section 73(a)(3) of Act 61 of 1973**

*We therefore suggest a review of referring to both genders in legislation.*

**Part 22: Amendment of section 269B of Act 61 of 1973**

*We suggest the deletion of the entire section as we believe that all public interest companies should be required to appoint an audit committee.*

**Part 24: Amendment of section 270A(5)(c) and (d) of Act 61 of 1973**

*This section should be amended to include a consideration of not only a professional and industry code but also compliance with the companies act. The companies act includes other more stringent audit requirements that might be found in a professional or industry code.*

**Part 28: Amendment of section 275(3) of Act 61 of 1973**

*We suggest that the audit should not be a mandatory requirement for private companies.*

**Part 29: Amendment of section 275A of Act 61 of 1973**

*We suggest that financial advisory services be included as one of the restricted services. We therefore suggest that auditors be required to publish their audited financial statements, as well as disclosure of fees generated by way of audit services and those generated by non-audit services. This information should also form part of the annual reports of public interest companies.*



**Part 33: Amendment of section 285A(c) of Act 61 of 1973**

*We request clarity on whether the word "fairly present" in this section will nullify the otherwise laudable provisions of sections 285A(a) and (b). Refer to our comments under **Part 7: Amendment of section 38 of Act 61 of 1973** and **General Comments: Part 1** in this regard.*

**Part 50: New section 440P in Act 61 of 1973**

*We therefore suggest the following changes:*

- (a) four persons registered with the IRBA and practising as registered auditors
- (c) two persons responsible for preparing financial statements for limited interest companies
- (d) two users of limited interest company financial statements; and two users of public interest company financial statements

**Part 50: New section 440Q(4) and in Act 61 of 1973**

*We suggest that the Council should from time to time be renewed with appropriately qualified persons that were not previous members of either the APB or the Council.*

**Part 50: New section 440W in Act 61 of 1973**

*We therefore suggest the following changes:*

- (b) six persons registered with the IRBA
- (c) six appropriately qualified persons that are members of a professional accountancy body.

**Part 50: New section 440X(4) and in Act 61 of 1973**

*We suggest that the Panel should from time to time be renewed with appropriately qualified persons that were not previous members of either the GAAP Monitoring Panel or the Panel.*

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**Part 5: Contributors (Draft Company Amendment Bill and/or Corporate Laws Amendment Bill)**

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## Part 6: SAIPA

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- The SAIPA is the second largest accounting institute in South Africa, boasting a membership of more than 6000, (excluding students and other associates) 78,5% of whom are in private practice.
- Close to 20% of the members of the SAIPA are black (African, Coloured or Indian)
- The SAIPA is a full voting member of the International Federation of Accountants (IFAC) as well as the East, Central and Southern African Federation of Accountants (ECSAFA).
- The SAIPA was the first Institute in South Africa to implement mandatory Continuous Development Programme (CPD) attendance and Professional Indemnity insurance protecting members of the public.
- SAIPA qualifications are recognized at level 7 by the National Qualifications Framework (NQF) in terms of the South African Qualifications Authority (SAQA).
- The SAIPA employs more than 20 staff members to operate as its secretariat. The highest decision making body of the Institute is its Board. Various committees support the work of the secretariat.
- Membership to the SAIPA is dependent on: obtaining a relevant degree; obtaining the necessary experience and competence to be recognized as professional accountant; and by successfully completing the Professional Evaluation as administered by the Institute. As a member of IFAC the Institute has to comply with the education and training requirements for professional accountants as determined by IFAC.
- SAIPA members act as professional accountants in business, private practice, government and academia.
- SAIPA members are recognized by statute, to issue statutory reports. These are issued for example, in terms of the: Micro lending industry regulations, Sectional Titles Act, Non Profit Organizations Act, Schools Act, Debt Collectors Act, Co-operatives Act, National Lottery Board Regulations, SABC Television Licensing Regulations, Immigration Regulations, Department of Trade and Industry's Industrial Development Programme, as well as the Close Corporations Act.
- SAIPA members are recognized, upon application, as Compliance Officers in terms of the Financial Advisory and Intermediary Services Act.
- SAIPA members are recognized as Commissioners of Oaths.