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Towards Improved Mechanisms to Hold Auditors and Auditing Firms Accountable for Money Laundering in South Africa: A Policy and Legislative Review

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ABSTRACT

The role of Auditing firms is crucial in that they ensure that company financial statements are accurate and reliable. However several high-profile corporate scandals that emerged in South Africa in recent years, have raised questions regarding the effectiveness of big auditing firms. As a result, there is growing concern about the need to hold auditing firms accountable for their actions. Big audit firms like Deloitte, EY, KPMG and PwC are alleged to have systemically being involved in economic crimes and State Capture committed in South Africa. The evidence presented in numerous reports such as the State Capture Report, suggests that prioritisation of profit over professional duties and the law has taken precedence by these firms.

Their involvement and allegiance to the Gupta Family in these scandals has had a costly impact on the South African government revenue. The Gupta family is alleged to be close to President Zuma, have managed to milk the South African Government about $7 billion. They also bought themselves a well-known Auditing Firm (Nkonki) to effect their agenda. Subsequently the Government instituted a State Capture Commission to investigate.

An analysis of some of the most atrocious corporate crimes committed by the Gupta enterprises can be easily found in many State Owned Entities but the prominently featured cases at the State Capture Commission are Eskom corruption Allegations, Transnet's tender of new locomotives and the FreeState Estina Dairy Project. In each case the role of auditing firms, accountants and lawyers is revealed not just as incidental to, but essential to setting up, facilitating and perpetuating elements of irregularity.

One main concern about these big auditing firms has been their close proximity to politicians and the companies they audit creating allegations of so called "information asymmetry" between them and the companies they audit. This has created assumptions of conflicts of interest that may have compromised the independence and objectivity of these audit firms. In some cases, auditors have been accused of turning a blind eye to fraudulent activities or failing to report them to the relevant authorities.

To address these concerns, there have been calls for greater transparency and accountability in the auditing profession. One proposal has been to give more power to the Independent Regulatory Board Authority (IRBA) tasked to oversee the work of auditors and ensure that they adhere to ethical and professional standards. Assuming that this would help to restore public trust in the auditing profession and ensure that companies are held accountable for their financial reporting.

Another proposal has been to increase the penalties for auditing firms that fail to meet their obligation to report any failures to comply with the country laws at the earliest moment, or raise concerns about their client's internal controls systems or their material financial misstatements, or lack of supporting evidence. The South African laws prescribes that both internal and external auditors should report any process flaws or suspicious transactions, such as inflated procurement pricing, overpayment, and non-delivery, which may pose a very high and significant risk to the company they are auditing. Currently, the penalties for non-compliance are relatively low, which may not be enough to deter auditors from engaging in unethical behavior. By increasing the penalties, the assumption is that the auditing firms will be more likely to be accountable and take their responsibilities seriously, ensuring that they are meeting their obligations to the public, and not sign financial statements without qualification or concern.

Either by design or by default, there has been assumptions that little action is taken by legal institutions to pursue auditing firms implicated in any of these lapses or misdemeanors. The belief is that the current legal system protects the activities of auditing firms from being

scrutinised. And that Government agencies tasked with upholding the law, lack experience and skills to can investigate the Auditing firms.

Considering that each country has a different definition of Money Laundering, and a different regulatory regime structure for investigating and prosecuting Money Laundering crimes. As such, in this research thesis, references to “Money Laundering” refers to any intentional criminal conduct that is intended to violate any country’s financial laws. For the purposes of this paper the Money laundering meaning is intended to be broad enough to accommodate the different legal definitions covered by different countries.

The research is meant to critically analyze issues and perspectives relating to the involvement of the auditing firms in these scandals, even though the issues involved are encountered globally by all auditing firms. To also look at the impact that the lack of oversight by these auditing firms has had on the South African economy and the audit profession itself.

LIST OF ACRONYMS:

ARA:	Assets Recovery Agency
BEPS:	Base Erosion and Profit Sharing
CPS:	Crown Prosecution Service
DPCI:	Directorate for Priority Crime Investigation
FICA:	Financial Intelligence Centre Act 38 of 2001
FIC:	Financial Intelligence Centre
FMA:	Financial Markets Act 19 0f 2012
GDP:	Gross Domestic Product
IFIAR:	International Forum of Independent Audit Regulators
IRBA:	Independent Regulatory Board for Auditors
KPMG:	Klynveld Peat Marwick Goerdeler.
NDPP:	National Director of Public Prosecutions
OCH:	Optimum Coal Holdings
OECD:	Organisation for Economic Co-operation and Development
POCA:	Prevention of Organised Crime Act 121 of 1998
PwC:	PricewaterhouseCoopers
RCPO:	Revenue and Customs Prosecution Office
SAICA:	South African Institute of Chartered Accountants
SCOPA:	The South African Standing Committee on Public Accounts
SFO:	Serious Fraud Office
SOCA:	Serious Organised Crime Agency
SOE:	State Owned Company
UK:	United Kingdom

CONTENT OUTLINE:

PART A- Introduction; CH1
PART B- Literature Review; CH2 &CH3 Legislation, Laundering and audit quality,
PART C- Data and methodology; CH4 &CH5 Case studies, a comparable study
PART D- Discussion and results; CH6 industry's Impact, CH7 Social Impact
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CHAPTER1.

1.1 INTRODUCTION:

Globally, the auditing profession has increasingly been confronted with a disturbing paradox and trust deficit. The lack of Professional skepticism and compliance with Ethical standards has become increasingly prevalent in institutions, as a result there are many corporate scandals that got reported in recent years (Skubinn & Herzog 2016).[1] South Africa was no exception, just after historical debacles such as the LeisureNet, Saambou, MacMed, Masterbond, and Regal Treasury Private Bank scandals were reported, new high-profile scandals erupted again. Big Auditing firms were scrutinised and accused of collusion in the emergence of these new high-profile corporate scandals that led to the establishment of a State Capture Enquiry by South African Government.

Amongst the new emerging scandals, the VBS Bank Closure, the corruption allegations at Eskom, The Steinhoff case of "accounting irregularities", the Transnet locomotives debacle, the classic Estina/Vrede Dairy Project case and many others. In-between the credible value of the audit function deteriorated to the lowest level ever due to the involvement of the big Audit Firms such that the Audit Profession ran the risk of extinction (Gloeck & De Jager 1998).[2]

South African companies would not be able to move huge amounts of money without the help of experts who can create the complex webs of transactions intended to conceal and obscure such activities. Companies engaged the services of professionals such as lawyers, accountants and auditors, whom by law are obliged by law to report fraud and money laundering at an earliest moment during the delivery of their services, yet they were alleged to be entangled in creating loopholes that make laundering of proceeds look legal and benefit such corporates.

Whether it is by design or by default, there is also a suggestion that there's reluctance and/or inability by legal institutions to pursue auditing firms implicated in these irregularities. There is a belief that "the current regulatory apparatus operates to shield the activities of auditing firms from critical scrutiny."[3] Thus the auditing firms are seen to be the law unto themselves since they are not audited by anyone.

This chapter intends to highlight the audit profession challenges faced in South African, to introduce the money laundering definitions, the background and history of money laundering, the significance and aim of the study, the problems identified, the research justification and context, and the research methods utilized. A brief literature review is also added.

1.2 DEFINITION OF MONEY LAUNDERING:

The meaning of the term, "money laundering," in simple terms refers to attempts of turning illegally gained money into legal and lawful money, disguising its original source and eliminating its flowing trail.

The Financial Intelligence Centre Act 38 of 2001 (FIC Act)[4] refers money laundering as an unlawful activity or any interest in such constituting an offence in terms of section 64 of the FIC Act.[5] In a similar tone, The Prevention of Organised Crime Act 121 of 1998 further

[1] Skubinn, R. & Herzog, L. 2016. Internalized moral identity in ethical leadership. Journal of Business Ethics, 133(2): 249-260.
[2] Gloeck, J.D & De Jager, H. 1998. *Seeking a brighter future for auditing in South Africa*. Pretoria: University of Pretoria.
[3] Lynley Donnelly,"Audit regulator refers irregularities found at Transnet, Eskom for investigation" Mail & Guardian (Johannesburg, 07 Jul 2017)
[4] Financial Intelligence Centre Act 38 of 2001, s64.
[5] Chinelle van der Westhuizen, 'Money laundering and the impact thereof on selected African Countries: A comparative study' (2011) < http://hdl.handle.net/2263/29700>

identifies a series of offences classified as money laundering.[6] The concept of Money Laundering and related counter legislation will be discussed in detail in Chapter 2.

The Prevention of Organised Crime Act 121 of 1998, The Financial Intelligence Centre Act 38 of 2001 (FICA), and The Companies Act 71 of 2008, form the basis of anti-money laundering (AML) legislative regime in South Africa. And many other supportive laws have also been established to close any gaps that may be identified, yet launderers still find other gaps to capitalize on with or without the help of professional such as auditors, lawyers and accountants.

1.3 PROBLEM STATEMENT:

It has become a critical challenge to understand, address and analyze the types of financial crimes committed by corporations, their nature and impact, and the role of auditing professionals in such activities resulting in adverse economic effects and political stability on many countries. The most critical challenge to understanding the impact thereof "is that its clandestine nature makes it difficult to observe'.[7] The nature and impacts of such crimes on a country's economic and political stability cannot be easily quantified nor under estimated.

Considering the scandals that have emerged in the past decade, it is therefore undeniable that auditing companies and individual auditors have been somehow involved in assisting in the irregularities by being negligence and dishonest in rendering their services internationally.

Based on these inferences, the possibility to identify the extent of the impact of such laundering activities, the involvement of the auditing firms, and a need to introduce interventions that requires auditors to play a central role in the detection and reporting of such crimes becomes an urgent necessity. This paper is about the roles and responsibilities of the Auditing professionals in terms of audit accountability, and it further establishes whether the disciplinary action taken against them, and the fines imposed, needs to be reviewed because they are assumed to be ineffective to inhibit fraudulent irregularities that are regarded to be reportable. Instead auditing firms would hide the extent of their culpability and agree to settle on penalties that they easily absorb as business cost.

1.4 RESEARCH AIM AND OBJECTIVES:

It is a well-known fact that the relationship between business and auditing firms has become so cozy that auditing firms are tempted to be too relaxed in the execution of their jobs. As such, most auditing firms seem to ignore complying with their ethical standards.

To a large degree, anti-money-laundering measures depend on auditing firms to report any suspected activities. The recent scandals have underscored the need to have measures in place to hold auditing firms accountable for their failure to execute their duties.
Within this backdrop, the objective of this research is to do the following:

- To provide an overview of the recent money laundering scandals in South Africa, with a view to highlighting the fact that these activities are on the rise.
- To conduct a review of the regulatory framework to combat these irregular activities by taking stock of both the policy and legislative measures currently in place, with a view to underscore the role of auditing firms under the current regulatory framework. Subsequently develop strategies intended to oversee adherence to professional standards by professional bodies.
- To conduct a comparative study of similar initiatives in other jurisdictions and measures put in place to hold auditing firms accountable for not reporting suspect irregular activities, drawing some lessons from the USA and UK.

[6] Mohammad Aslani, "Financial Crimes Auditing" (2012). <http://www.ijtef.org/papers/169-N10004.pdf>
[7] Moshi, "Fighting Money laundering: The challenges in Africa" (2007) 3, ISS Paper 152.

- To propose and recommend measures that can be adopted in South Africa to hold auditing firms accountable based on an analysis of some of the gaps and lapses that have emerged.

The thesis seeks to improve and clarify the role of auditing in detection and reporting suspect activities and provide valuable input for further investigation on the topic.

The researcher intends to contribute to the advancement of audit knowledge, the audit accountability literature, the auditing research, and legal accounting. He further intends to explore an ideal opportunity that presents itself in the auditing industry today, by providing insight into Gupta related scandals and the auditing firms involved. Also to provide the impact that audit reports have on suspect irregular activities by the said clients, and to relook at the regulatory policy and legislative framework governing the auditing firms with a view to strengthening accountability measures. And lastly to review and consider whether the disciplinary actions and fines imposed upon auditing firms and the auditors involved are severe enough to inhibit such actions.

1.5 RESEARCH QUESTIONS:

Considering the issues raised in the problem statement, the following research questions are to be addressed:

- Do South African auditors lack the required degree of independence and professional scepticism?
- Is there a need to strengthen current regulations and policies to effectively hold auditing firms accountable?
- Are fines and disciplinary actions imposed upon auditing firms and the auditors involved, severe enough to force them to report RIs and inhibit fraudulent transactions?

1.6 JUSTIFICATION AND CONTEXT:

The role of auditing in the detection and reporting of money laundering and white-collar crime in general has never being so relevant and important in both deterrence and detection of such crimes. Yet so little has been investigated on the role that audit firms allegedly play as accessory to such activities by pushing such under the carpet. Little to not enough research has been done on the complicity of auditing firms in money laundering and lack of credible audit outputs especially on big corporations because government's lack enough capacity to can deal with these firms, and contemplated punitive measures to be taken not only against auditors but also the auditing firms themselves is found to be wanting.

The recent corporate scandals have auditing firms largely embroiled in the spotlight justifying scrutiny of their practices in the public interest. Various incidents have revealed the central role that some auditing firms have played in serious illegal governance-flouting acts instead of ensuring public accountability and transparency of their clients. These incidents have necessitated scrutiny and research around these questionable governance practices.

To mention a few incidents uncovered In South Africa:

- KPMG involvement with the Gupta Family businesses, and the resultant damage that have resulted to the auditing profession and the country.
- McKinsey's engagement in bribery and claims for so-called professional services that they never rendered.
- McKinsey's corruption allegations and the use of companies like Trillian as money laundering conduits.
- The Steinhoff Investment Holdings case of "accounting irregularities".

- Ernst & Young being accused of ignoring serious governance-flouting findings observed at Transnet, a state utility, accused of cover-up of its procurement irregularities that resulted in R5.4-billion overspending on its capital expansion program.
- KPMG's 2005 deferred prosecution agreement (DPA) with the Department of Justice (DOJ) for its questionable audit practices and involvement in the marketing of questionable tax shelters.

The involved auditing firms have been found to be helping their clients in promoting financial secrecy and complexity which forms the basis of massive revenue losses to the state and profit shifting that impose enormous social costs through cuts in public spending instead of leading in reporting these as suspect fraudulent and irregular activities at a first glance. On the other side, either by default or by design, they seem to escape criminal or civil liability for being complicit in their negligent auditing practices to the disgruntled shareholders.

Now, more than ever there has been a need to raise and improve on the auditing ethical standards, the industry's self-regulation, and the need to review related statutory regulations to be at par with global standards. This thesis will lay basis for further research more especially from a South African context to can relook at how the auditing profession can be brought to account for the shoddy work.

1.7 RESEARCH METHODOLOGY:

The researcher will adopt a desktop study methodology, drawing on a range of secondary research sources to demonstrate how auditing firm's activities in some companies involve willful lack of oversight to complicity in dubious and fraudulent activities.

The author has made use of an already accumulated bank of vast knowledge including but not limited to:

- Legislation relating to Money Laundering and regulation of the audit function,
- Case law,
- Investigative Journalistic articles on specific companies involving Big Auditing Firms,
- Various Commissions reports, Publications of International Institutions, and investigations on practices by various Auditing Firms,
- Manuscripts and Scholarly Articles on the topic,
- Information from compliance related organizations and Independent Watchdogs,
- Legal recommendations such as Kings Reports,
- Books on the subject matter,
- Credible online articles.

All these tools will be used to identify the alleged involvement of auditing firms in helping corporate irregular behavior that lead to tax base erosion and destabilization of the South African economy. Because document analysis forms the basis of findings and conclusions of this research, little interaction with people involved was undertaken considering there was no infringing into their privacy or need for their consent.

1.8 DATA COLLECTION:

The following case studies implicating auditing professionals and their employers of negligence and dishonest practices were reviewed and analysed:

- The Steinhoff case involving Deloitte and Touche, PWC,
- The VBS Mutual Bank case involving KPMG,
- The Transnet case involving KPMG, McKinsey, and Ernest & Young,
- The Eskom case involving PWC, Nkonki and McKinsey,
- The Estina Dairy project involving KPMG,
- The Ntsebeza (SARS) Inquiry involving KPMG,

1.9 LITERATURE REVIEW:

For the purposes of this research, it is clear that the existing literature would not assist in resolving the currently developing dynamics involvement of auditing firms in allegations levelled against the Gupta family and their companies in the alleged money laundering activities that has given rise to state capture allegations. The current literature would not address the current investigations but is rather based on past experiences and existing empirical data. None the less, there is a few authors and researchers that have already started to look at the developing dynamics making headlines in South Africa considering these are news making issues touching on public interest. The South African government and its relevant legal entities are investigating these matters, including few enquiries being established.

The South African Government and its citizens are increasingly seeing corruption and money laundering as one of the most important issues hampering the newly found democracy. They have seen an increase in alleged laundering incidents, corruption and fraud since the advent of democracy in 1994 involving highly placed politicians and professionals. In 2008, the then President of the country, Jacob Zuma was accused of a number of allegations including: racketeering, money laundering and fraud (Gumede: 2008)[8]. He was subsequently acquitted but the charges were recently reinstated.

Reports such as the Irish Government Publications 2000 confirmed that the ineffective regulatory regimes were the causes of detraction from the audit function values, and thus undermine public confidence in the profession as a whole (Land 1995; Gloeck & De Jager 1998; Gray & Manson 2000;).[9] Porter also refers to the many ethical lapses experienced in the audit industry as performance expectation differences between auditors and clients (Porter, HÓgartaigh & Baskerville 2012; The Economist 2018b),[10] He attributes these lapses to a deterioration in professional values of independence, objectivity, competence and maintenance of ethical standards and professional skepticism (Hurtt et al. 2013).[11] With professional skepticism defined as an indispensable auditor characteristic that is inclusive of a questioning mindset and a critical assessment of audit evidence (Chen et al. 2012)[12]. This skepticism requires auditors to exercise due diligence and a high standard of care that drives them to recognise potential errors and irregularities, and to investigate misstatements (Glover & Prawitt 2014).[13]

Whilst Lodge (2002)[14] refers to a survey that was conducted in 1998 where 55 percent of the population answered that they thought that highly placed civil servants took bribes. This has hampered service delivery programs and thus led to civil protests. The South African media with the use of investigative journalism has been instrumental in exposing most of these scandals and thus put pressure on government to investigate. A few project reports have started to trickle in, allowing experts to have a basis to can start researching and coming up with proposed solutions. Chikeleze and Baehrend notes that over the past decade, the experienced ethical failures by organizations brought about the interest to promote ethical conduct and develop ethical leaders (Chikeleze and Baehrend (2017:45)).[15]

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[8] Gumede, W. M. '*South Africa: Jacob Zuma and the Difficulties of Consolidating South Africa's Democracy*.' (*African Affairs*, 107, 261-271)

[9] Land, N. 1995. The future of audit regulation. Accountancy. July:92-93.

[10] Porter, B., HÓgartaigh, C. & Baskerville, R., 2012, 'Audit expectation-performance gap revisited: Evidence from New Zealand and the United Kingdom', International Journal of Auditing 16(3), 215–247. https://doi.org/10.1111/j.1099-1123.2011.00444.x

[11] Hurtt, R. K. Brown-Liburd, H. Earley, C. E. & Krishnamoorthy, G. 2013. Research on auditor professional skepticism: Literature synthesis and opportunities for future research. Auditing: A Journal of Practice & Theory, 32(Sp 1), 45–97.

[12] Chen, Q. Kelly, K. & Salterio, S. E. (2012). Do changes in audit actions and attitudes consistent with increased auditor skepticism deter aggressive earnings management? An experimental investigation. Accounting, Organizations and Society, 37(2), 95–115.

[13] Glover, S.M. Prawitt, D.F. 2014, 'Enhancing auditor professional skepticism: The professional skepticism continuum', Current Issues in Auditing 8(2), P1–P10. https://doi.org/10.2308/ciia-50895

[14] Lodge, T. (2002). "*Political Corruption in South Africa: From Apartheid to Multiracial State*." (In A. Heidenheimer, & M. Johnson (Eds.), Political Corruption: Concepts and Contexts (pp. 403-424). New Brunswick, NJ.)

[15] Chikeleze, M.C. & Baehrend, W.R. 2017. Ethical leadership style and its impact on decision-making. *Journal of Leadership Studies*, 11(2):45-47.

Considering there is little academic material on the alleged complicity of auditors in a South African context, other sources of data such as governmental reports, non-governmental reports and journalistic articles have been used to draw evidence pertaining to suspect irregular activities, dishonest practices and negligent behaviour by auditing firms and their employees. The State Capture Report and IRBA Reports have also been used, and in the case of VBS Mutual Bank and other SoEs, governmental reports and media reports have been used as a source of data, considering these are new developments and there is not yet any academic material to be used.

Bowen (2009)[16] recommends the use of organisational or institutional reports, press releases, and other various public records as documentary research evidence. The author therefore used as the basis for his research reports such as:

- Mark Swilling: *"Betrayal of the promise: How South Africa is being stolen."* The State Capacity Research Project, 2017.[17]
- Financial Intelligence Centre (FIC) annual report for 2016/17.[18]
- Independent Regulatory Board for Auditors. Combating Money Laundering and Financing of Terrorism*: "A Guide for Registered Auditors."* 2011.[19]

As these reports and other research papers gather momentum, a new literature cache could be developed which could also inform future legislation. These reports, new literature cache and related journals have been used and analysed to give detail to the phenomenon of fraudulent transactions, money laundering, negligence and dishonest practices committed.

While there has been also some research on the legislative shortcomings on this topic in other countries such as the U.S.A and UK, the enactment of the Sarbanes Oxley Act (2002) (SOX) in the USA, and other legal enactments in the UK and Other EU countries, serves as an excellent example to look at. As far as African economies are concerned, little is known about comparative efforts at improving audit practice (Humphrey et al, 2011).[20]

Following on the developments in South Africa, numerous SADC governments have also chosen a zero tolerance approach to curb this scourge. This is driven through the establishment of organisations such as the East and Southern African Anti-Money Laundering Group (ESAAMLAG). The existence of such formations brings hope even though there are still big concerns to be addressed. Such as the fact that there still yet to be people that are prosecution for big money laundering scandals in any of these countries, since enforcement agencies being under capacitated, underfunded, untrained. With all these hurdles, the fight against money laundering seem ominous.

None the less, the research does a comparative study of similar initiatives in many other jurisdictions, and preventative measures undertaken to prevent further professional gaps in Chapter 5. Cases like the Carillion case study are used since involving all the big 4 auditing

[16] Bowen, G.A. 2009. Document analysis as a qualitative research Method. Qualitative Research Journal, 9(2): 27-40.
[17] Mark Swilling: *"Betrayal of the promise: How South Africa is being stolen."* The State Capacity Research Project. 2017 <http://pari.org.za/wp-content/uploads/2017/05/Betrayal-of-the-Promise-25052017.pdf>
[18] Financial Intelligence Centre (FIC) annual report for 2016/17 <https://www.fic.gov.za/Documents/FIC%20Annual%20Report%202016-17%20(LR).pdf>
[19] Independent Regulatory Board for Auditors. 2011. Combating Money Laundering and Financing of Terrorism: "A Guide for Registered Auditors." <https://www.irba.co.za/upload/irba-guide-for-ras-combating-money-laundering(1).pdf>
[20] Humphrey, C., Kokali, S. and Samsonova, A. (2011) The politics of transnational policy making: inpursuit of auditor liability limitation in the EU, Working Paper, Manchester Accounting andFinance Group (MAFG), Manchester Business School

firms shenanigans in a conflict of interest as they had failed to caution against corporate disasters such as Carillion (Pickard:2018).[21]

1.10. LIMITATIONS OF THE STUDY:

Although the research is limited to South African scandals, a comparison to similar global incidents emerging in other developing economies will be highlighted to offer a comparable insight into similar established economies. The lack of information available to legislators, and lack of accurate cost estimate of the impact or extent of effect of money laundering in any particular country, poses limitations to a better understanding the topic.

1.11 CONCLUSION:

The chapter highlighted the audit profession challenges faced in South African. It introduced money laundering definitions, the background and history of money laundering. Discussion was also made of the significance and objective of the study and related problems. The research justification and context, and the research methods utilized were also delved into. The research literature review and research methods were briefly discussed.

The researcher explained his reasons to choose a qualitative approach for the study. Considering the problem issues raised questions were identified with reference to professional scepticism and independence.A need to strengthen current regulations and policies, and whether disciplinary actions and fines imposed are severe enough to inhibit irregular behavior?

Mention was made in short of Money Laundering Control Legislation and processes and actions adopted by legislators to discourage irregular practices which will be further discussed in detail in Chapter2. Mention was also made of incidences of negligence or irregular practices implicating a number of auditing firms and Professional auditors which will be discussed in Chapter4.

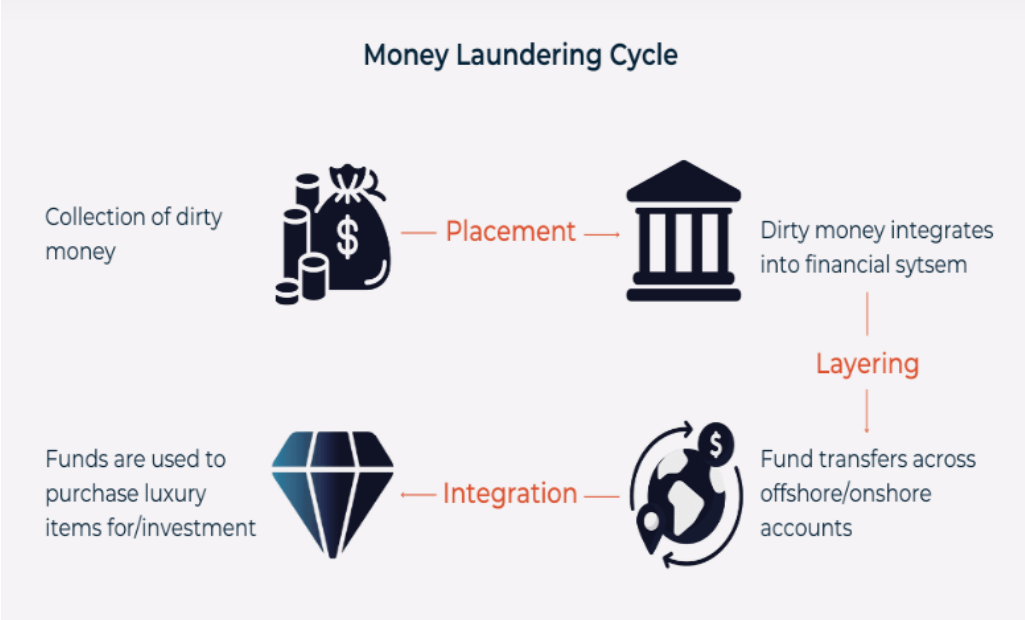
[21] Pickard, Jim, and Madison Marriage. 2018. Labour Consider Breaking up Big Four Auditing Firms. The Financial Times. September 21. Available online: https://www.ft.com/content/43fbd564-bc30-11e8-94b2-17176fbf93f5 (accessed on 12 December 2018).

CHAPTER 2: Money laundering control.

2.1 INTRODUCTION:

Money laundering cases around the world have been systematically analyzed thoroughly and seriously, since the processes involved in laundering have evolved and became cumbersome with each case involved. The common features found with each case were: hiding the origins of the funds, possession of the proceeds thereof, using sophisticated methods and constant pursuit of profit to transform those proceeds. The process of laundering in most cases occurs in three stages: i.e. placement, layering and integration stage:[22]

- **Placement:** refers to the "dirty money" being injecting into the legitimate financial system either sending the illicit funds to an offshore account and thereafter return it through correct channels, or smurfing which involves dividing the money into pieces and deposit it in multiple bank accounts, or use invoicing for non-existing goods or services.
- **Layering:** refers to concealing the source and audit trail of the illicit funds by layering a series of transactions using legal bookkeeping tricks taking advantage of legal gaps or buying shares or property with the illicit money
- **Integration:** refers to reintegration of the now laundered money by disbursing it from a legitimate account to the launderer's accounts using methods such as invoicing to be used legitimately to buy properties and/or legally invest.



Pic: Compliments of Sanction-Scanner

It is common practice that as long as there is a constant pursuit of profit, money laundering will take place in one form or another. The 4th IR era has come with its problems and money launderers have also adopted advanced technological methods in their pursuit, and are engaging professional assistance like the use of lawyers and accountants in transnational movement of funds. Thus taking advantage of differences in tax laws and existence of tax havens offered by different countries.

[22] Alyssa Abrams. The Three Stages of Money Laundering and How Money Laundering Impacts Business. The SumSuber. Apr 25, 2024

This chapter will explain money laundering as a concept, the Control efforts undertaken and related jurisprudence meant to curb the crime. It will also outline the South African AML regulatory framework and the laws governing the audit work. The writer will also look at laws, ethical codes, requirements to join the profession and related professional bodies, and the standards and norms to be adhered to.

2.2 CONCEPT OF MONEY LAUNDERING:

Section 1 of the FICA (2001),[23] a primary money laundering control statute in South Africa, refers to the concept of money laundering as:

> *'An activity which has or is likely to have the effect of concealing or disguising the nature, source, location, disposition or movement of the proceeds of unlawful activities or any interest which anyone has in such proceeds……'*[24]

Whilst Section 1(xv) of the Prevention of Organised Crime Act 121,[25] refers to 'proceeds' of unlawful activities whether done in South Africa or abroad as:

> *'any property or any service, advantage, benefit or reward which was derived, received or retained, directly or indirectly, in connection with or as a result of any unlawful activity carried on by any person'*[26]

Thus it can be deduced that money laundering is a process used by criminals to conceal the origin or ownership of the benefits of crime, or the illegal nature of a financial transaction.[27] One can deduce four elements form this definition, that is: a process, the objective or intention of such process, the intended outcome and ultimate goal of such an activity.

In lay man terms, laundering can only occur once a person benefits from criminal offences such as shoddy deals and bank transfers, as soon as the money has been cleaned and cleared through a legal financial system. The definition includes people who, knowingly or ought to have reasonably known, that such proceeds forms part of criminal activities, instead engaged or agrees to assist that person to acquire, possess and benefit in use such proceeds.

Money laundering also has an international character. In order to explain this a case in point is the failure of the Bank of Credit and Commerce International (BCCI).[28] The BCCI was used to launder money for both terrorists and world intelligence agencies. It was a joint venture set up between a Pakistani banker called Aga Hassan Abedi and the Bank of America in 1972, with its main office based in London in an attempt to prevent nationalization.

The bank was a fraud and was regulated nowhere from the start because it had no legitimate capital. This bank created one of the most complex deceptions in banking history. Something its auditors, PWC, discovered later and describe it as one of the largest scam they had ever encountered. The auditors alleged that some transactions on BCCI's accounts were 'false or deceitful' and Swaleh Naqvi (the BCCI CEO) subsequently resigned and Aga Hassan Abedi severed ties with the bank also.

The Bank was linked to many unsavory customers and made suspicious loans, concealed deposits, misstated its financials, and had dictators, terrorists, spies and drug runners as its customers. The revelations raised a lot of questions about how a financial scandal of such magnitude could not have been discovered, and how come auditors could claim not to have

[23] SOUTH AFRICA. 2005. The Financial Intelligence Centre Act 38 of 2001. Pretoria: Government Printer.
[24] SOUTH AFRICA. 2005. The Financial Intelligence Centre Act 38 of 2001. Pretoria: Government Printer.
[25] SOUTH AFRICA. 1998. Prevention of Organised Crime Act 121 of 1998, (POCA). Pretoria: Government Printer.
[26] POCA *op sit*
[27] Savona & De Feo International Money Laundering Trends.
[28] Passas, N. I Cheat, Therefore I Exist: The BCCI Scandal in Context. In W.M. Hofman, J. Kamm, R.E. Frederick & E. Petry (Eds),International Perspectives on Business Ethics. New York: Quorum Books, 1993.

seen and reported it? Ultimately the Bank of England wound it down and closed it, alleging that it had committed massive fraud and could not be reformed.

2.3 MONEY LAUNDERING CONTROL LEGISLATION IN SOUTH AFRICA:

Money laundering is one big challenge facing world governments today, which is not an exceptional problem to South Africa. The incident of money laundering, corruption and fraud has been on the increase since the advent of South African democracy in 1994, and this has not been complimented by the criminal charges pressed against those implicated. This imbalance can be ascribed to high position political officials and police who are involved in such corrupt activities.

The lack of Professional and Ethical standards in the audit industry has become increasingly prevalent due to the many scandals that have been reported in recent years (Skubinn & Herzog 2016).[29] More new scandals emerged after historical debacles such as the Masterbond, Saambou, LeisureNet, Regal Treasury Private Bank, and MacMed scandal. These scandals precipitated a review of regulations and promulgation of a few new legislations, which are discussed in detail here underneath. Some of which were either promulgated or amended specifically to curb the scourge of criminal actions related to laundering. Here are some of the primary South African statutory pieces that regulate anti money laundering and terrorist financing crimes:

2.3.1 The Companies Act No.71 of 2008 (the "Companies Act"): is the primary law that governs company incorporation and registration whose aim is:

- To encourage transparency and corporate governance,
- To balance shareholder's and director's obligations and rights, and
- To provide legal redress for third parties in respect to companies and the board of directors irregularities.

The Act prescribes relations between companies, shareholders, and the fiduciary duties and prescribed standards of financial reporting by directors. It also prescribes procedures for shareholder general meetings and how they should vote on company matters such as the appointment of directors or company auditors. This Act, as well as the South African common law also define the directors' basic duties and responsibilities, inclusive of the fiduciary duty of always acting in the best interests of the company and in good faith, with due care, diligence and skillfully.

Section 114(2) of the Act further provides for specific requirements for experts like auditors, to meet when about to share their opinion or about to exercise their judgment or make fair and just decisions on company matters they indulged in. The Act further expects auditors to abide by their professional codes of conduct and ethical practices.

The Companies Act requires the auditor to attest to the fairness of the financial statements he has audited, whilst it requires the company management to:

- Keep company's records safe (section 28 (1)),
- Avoid misstatements in company financials as this is an offence (ssection 28 (3)), and
- Present and explain the company's business and its financial position, (section 29 (1) (c)).

[29] Skubinn, R. & Herzog, L. 2016. Internalized moral identity in ethical leadership. Journal of Business Ethics, 133(2): 249-260.

Section 29 (2) of the Act prohibits companies from preparing misleading financial statements. Whilst section 29 (6) of the Act defines as a punishable crime the willful preparation, approval, dissemination or publication of misleading and false financial statements. Naudé, in his discussions about the Steinhoff case, defines the word "approval" to include the auditor's attestation, which if done with the knowledge that the financials attested to are materially false or misleading and noncompliant with the provisions of the law, becomes a criminal offense.[30]

The above mentioned statutory provisions were considered In Tonkwane Sawmill Co Ltd v Filmalter 1975. Boshoff J, in this case refers the auditor's position on detection of fraud and fair financial reporting, as follows:

> *"An audit is not a substitute for management control and no guarantee is given or to be implied that an audit will necessarily disclose fraudulent misappropriation."*[31]

2.3.2 Prevention of Organised Crime Act 121 of 1998: The Act intends to introduce measures aimed at combating organised crime, prohibiting activities relating to racketeering, criminalise activities aimed at concealing the nature, source, location, disposition or movement of criminal benefits, and provide for the seizure, confiscation and forfeiture of such benefits of crime to the state (Van Jaarsveld Izelde Louise, 2011).[32] At the core of this regulation is to correcting information asymmetries that crime impact has on civil liberties.

2.3.3 The Financial Intelligence Centre Act 38 of 2001 (FIC Act): The Act concerns itself with anti-money laundering control obligations including the duty to identify and know your clients, a duty to keep all records of transactions, the duty to report any irregularities, and all legal compliance duties.

The Financial Intelligence Center (FIC) is the country's national center for the production of financial intelligence. The center is responsible for identifying criminal proceeds and combating of money laundering by attempts of cleaning it through the Banks. The Act ensures that the financial systems are transparent by requiring financial and other institutions (identified in Schedule 1 and 3 of the FIC Act)[33] to apply customer due diligence measures in dealing with their clients. Adequately capturing customer information in their records and sharing that information, in case of suspect money laundering investigations. Some of these businesses are high-risk for money laundering activities, considering that some of these financial institutions are exposed to potential exploitation by criminals looking for ways to launder criminal proceeds.

FICA shares this information with other competent authorities like the South African Revenue Service (SARS) and law enforcement authorities for control purposes. Section 21(1) of The FIC Act[34] further requires auditing and Auditing Firms to have a good knowledge of their customers, as well as the understanding of the business that their customers are involved in. This compliance and customer due diligence measures makes it more difficult for criminals to launder money, because the accountable Institutions are required to regularly submit Suspicious Transaction Reports (STRs) to relevant authorities.

[30] Naudé, P, Hamilton, B. & Ungerer, M. 2018. Business Perspectives on the Steinhoff Saga. Cape Town.
[31] Tonkwane Sawmill Co Ltd v Filmalter 1975 (2) SA 453 (W).
[32] Izelde Louise Van Jaarsveld, *"Aspects of money laundering in South African law"* (2011) University of South Africa, Pretoria, <http://hdl.handle.net/10500/5091>
[33] SOUTH AFRICA. 2005. The Financial Intelligence Centre Act 38 of 2001. Pretoria: Government Printer.
[34] SOUTH AFRICA. 2005. The Financial Intelligence Centre Act 38 of 2001. Pretoria: Government Printer.

Section 29 of the FICA imposes the duty to report suspicious and unusual transactions or activities on certain persons to authorities. This obligation is imposed on business owners, managers and other employees contracted with the business. The obligation to report arises when a person knowingly or ought to have reasonably known or suspected that certain unlawful activities were undertaken in that business.

Information acquired from the auditing professionals could generate leads which may result in section 34 FIC Act directives to freeze any suspect proceeds acquired illegally, and section 35 applications meant for monitoring any use of such proceeds.

The FIC Act as amended is aligned and follows the principles set by International Anti-Money Laundering Regulations. As a result, the "know your customer" standard obligations are incorporated in the Act. The FIC Act and the POCA work hand in hand because whilst POCA deals with the actual offences, the FIC Act deals with administrative framework of regulating money laundering. The FIC Act has also been amended to include combating terrorism financing by POCDATARA.

The amendments to the FIC Act came about as a result of a peer review exercises done on a country's anti-money laundering regime by the Financial Action Task Force (FATF), of which South Africa is the only African member. The country is also a signatory to the UN Convention against Trans National Organised Crime and participates in regional and global structures established to deal with and eliminate money laundering. All these efforts together with strong auditing and reporting framework are associated to internationally accepted standards, and they gives the country the upper hand in anti-money laundering efforts.

2.3.4 The Protection of Constitutional Democracy against Terrorists and Related Activities Act 33 of 2004 (POCDATARA) addresses issues relating to the combating of terrorism. This is a highly complex and technical law. It must be read in tandem with POCA and the FIC Act since it amends certain provisions of the two Acts. Auditing professionals are required to consult it to determine the impact of the Act on their activities and are expected to report any impropriety associated with terrorism and related activities.[35]

2.3.5 Prevention and Combating of Corrupt Activities Act 12 of 2004: The PCCA applies to all organisations based inside and outside the country as long as they doing business in the country. It commenced to be operational in April 2004. The Act governs anti-bribery, prevention corruption and law enforcement in South Africa. The Act serves as the central point of the overall Anti-Bribery Compliance in South Africa, and serves to amend all previous legislation and international conventions.

The objectives of the Act are to strengthen corruption preventative measures, combat and criminalise all corrupt activities, deal with related investigations and create a register to blacklist offenders from getting government tenders, to impose the duty to report corrupt transactions by authorities, and prevent corrupt people from using their influence to spread corruption to other countries.

Section 34 of this Act[36] imposes the duty to report irregular offences on individuals holding positions of authority, if they know or should reasonably have known or suspects that criminal offences are being committed, or that irregular acts of theft, fraud, extortion or forgery, and

[35] L. De Koker; *South African money laundering and terror financing law*. (Butterworths LexisNexis.1999, chapter4.)
[36] Prevention and Combating of Corrupt Activities Act 12 of 2004

corruption involving R100 000 or more are being committed. It is a criminal offence not to report such, and carries a penalty of a fine, or a jail term of up to 10 years.

2.3.6 Proceeds of Crime Act 76 of 1996: Is meant to introduce measures to combat organised crime, gang activities, money laundering and racketeering. It criminalises certain activities associated with crime, and enforce an obligation to report certain illegal activities and to provide information connected therewith.

Chapter 5 of the POCA gives powers to criminal courts to empower law enforcement authorities to confiscate proceeds of crimes that are suspected to be beneficial to criminals. Such an order is meant to deprive beneficiation by the defendant of the proceeds of his crimes. Any prosecution made under an order attained under POCA requires the prosecution to only prove that the property or income attained were proceeds of a criminal activity.

2.4 MONEY LAUNDERING CONTROL OBLIGATIONS IN SOUTH AFRICA:

The money laundering control obligations identified by the FIC Act include a duty to identify and know your clients[37], a duty to keep business transactions records,[38] a duty to report suspicious transactions[39], and most importantly a duty to comply with the laws of the country.[40]

In terms of section 29 of the FIC Act, accountants, auditors and any service providers has a duty to report unusual and suspicious known transactions to the FIC, especially on suspicious transactions that exceed R25.000. These duties prescribed in section 29 of the FIC Act apply to all citizens.

Section 1 (2) (b) of the FIC Act clearly defines how the courts will infer a person to have known and willfully turned a blind eye to a known suspicious irregularity if:

> *(b) The court is satisfied that—*
> *(i) the person believes that there is a reasonable possibility of the existence of that fact; and*
> *(ii) the person fails to obtain information to confirm or refute the existence of that fact.*[41]

"Suspicion" is further clarified in *Frankel Pollak Vindirine Inc v Stanton* (1996) where the court held that:

> *"Where a person has a suspicion and deliberately refrains from making inquiries to determine whether it is groundless …… chooses to ignore them, it cannot be said that there is an absence of knowledge of what is suspected or warned against."*[42]

Section 30(2) of the FIC Act prescribes that any person or institution commits an offence if they do not report suspect transfers of cash into or out of South Africa in accordance to section 30(1) (Section 54). This means that any person intending to do cash transfers in excess of a prescribed minimums to or from South Africa has an obligation to report such transaction to Government prior transferring.

The duty to report suspicious acts of intended terrorism and related offences is also captured in section 12(1) of POCDATAR. It refers:

[37] Financial Intelligence Centre Act 38 of 2001, s 21(1)
[38] Financial Intelligence Centre Act 38 of 2001, chapter 1-3
[39] Financial Intelligence Centre Act 38 of 2001, s 29
[40] South African Law Commission: *Money Laundering and related Matters* (Projects 104, 1996)
[41] Financial Intelligence Centre Act 38 of 2001, s 21(2)(b)
[42] *Frankel Pollak Vindirine Inc v Stanton* [1996] 2 All SA 582 (W) 596c-d

12. (1) Any person who:

> *(a) has reason to suspect that any other person intends to commit or has committed an offence referred to in this chapter; or*
> *(b) is aware of the presence at any place of any other person who is so suspected of intending to commit or having committed such an offence, Must report as soon as reasonably possible such suspicion or presence, as the case may be, or cause such suspicion to be reported to any police official.*[43]

This section of this Act is clearly further emphasizing the importance of expectations by auditors to report their suspicions to the police as is also prescribed in terms of section 1 and section 29 of the FIC ACT which further refers to company employees.

In case the client fails to report, a registered auditor may file a reportable irregularity as is required and prescribed by section 45 of the Auditing Profession Act (APA) and the guidance issued by IRBA[44] which provides guidance on the interpretation and compliance relating to reportable irregularities.

Previously various money laundering cases that include accountants have been successfully prosecuted in South Africa, and convicted individuals given prison sentences. A classic example is that of State v Maddock Incorporated and Maddock, [45] in which case the two were prosecuted for money laundering and failure to comply with FIC Act. The accountant was found guilty for failing to report suspicious and unusual transactions and was given a jail sentence of 10 years.

2.5 MONEY MOVEMENT AND LAUNDERING IN SOUTH AFRICA:

In many instances the money laundering process involves organized criminal activities such as misrepresentation of an entity's financial statements, terrorism financing, drug trafficking, tax evasion, and deliberate bankruptcy misreporting.(Mc Dowell, 2001).[46]

The process of money laundering involves a series of multiple transactions guised in different ways and meant to hide the original source with an intention to finally integrating the money with legitimate funds and ultimately use the funds. The well-known guises are either incoming money laundering, or outgoing money laundering, or localised money laundering.

2.5.1 Incoming money laundering refers to illicit funds created outside the country and proceeds of such imported into the country. In the case of *State v Selebi*,[47] Mr. Selebi, a National Commissioner of the South African Police Services was accused of being involved in a generally corrupt relationship with Mr. Glen Norbert Agliotti, a European wanted criminal accused of using money from Europe to further his criminal activities in South Africa. The Commissioner shared secret information about Mr. Agliotti being investigated by UK law enforcement authorities, in return of bribes received from Mr. Agliotti. Selebi was found guilty and sentenced to 15 years imprisonment for corruption and contravening s 4(1) (a) of the Prevention and Combating of Corrupt Activities Act, 12 of 2004.

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[43] Protection of Constitutional Democracy against Terrorist and Related Activities Act, 2004 (Act No 33 of 2004) (POCDATAR), section 12(1)
[44] IRBA, "*Reportable Irregularities: A Guide for Registered Auditors*," (issued 30 June 2006)
[45] *State v Maddock Incorporated and Maddock*, Case SH7/17/08
[46] John McDowell, *Economic Perspectives* (Volume:6 Issue:2. 2001) Pages:6 to 8 https://www.ncjrs.gov/App/Publications/abstract.aspx?ID=191327
[47] State *v* Selebi (25/2009[2010] ZAGPJHC 53 (5 July 2010).

2.5.2 Outgoing money laundering refers to money made in South Africa and then brought to another country for laundering purposes. A typical example is that of a case of the *State v Gayadin*[48] in which a man was convicted of laundering R11 million under POCA 121 of 1998. He operated illegal casinos and with the help of accounting experts, laundered proceeds of these businesses by hiding money in offshore bank accounts on the Isle of Man and Jersey.

2.5.3 Localised money laundering refers to money being laundered and proceeds of such being disbursed within the country. In such cases criminals use business activities and legitimate businesses such or trusts to launder money. They will spend the money on expensive clothes, real estates, personal effects, or material things like vehicles, yachts, property and furniture, farms and livestock and in all these instances, all they want to achieve is to enjoy the benefit from their criminal proceeds and improve their lifestyle.

In a classic case of the biggest robbery that ever happened in South Africa, the *State v Dustigar* case[49] which involved professionals such as; a practicing attorney who used his trust account to hide some of the money, a police captain who created a laundering scheme. 19 people were convicted in this case. Most of them were relatives and friends who's bank accounts were used for money laundering activities. Some of these accounts were used to purchase properties with illicit funds.

2.6 SUSPICIOUS AND UNUSUAL TRANSACTIONS:

Section 29 of the FIC Act enforces the reporting of suspicious and unusual transactions to the FIC by accounting and reporting institutions, or any person who knows or discovers a suspicious financial transaction that looks like a potential money laundering activity. This is a very important element in international attempts to foster anti-money laundering activities by world countries. Recommendation 20 of the Financial Action Task Force ("the FATF") on Money Laundering refer:

> *"If financial institutions suspect that funds stem from criminal activity, they should be required to report promptly their suspicions to the competent authorities".*[50]

The list of suspect transactions that are reportable is not exhaustive but covers the activities such as unusual business transactions such as:

- Expedited deposits or transfers with little explanation,
- Unexplained international transfers,
- Excessive payments or high commissions,
- Large transfers to offshore accounts,
- Unexplained transfers into trusts and corporate vehicles,
- Selling or buying securities,
- Inconsistent large payments affecting liquidity of the firm and many more similar activities.

S 7(5)(a) of POCA 121of 1998, repealed by Section 29 of the FIC Act, had defined the general duty by all citizens to report any suspicious activities by anyone, with one exemption, the

[48] State *v* Gayadin Unreported (Case no 41/900/01, Regional Court, Durban)
[49] In State *v* Dustigar (Unreported Case no. CC6/2000, Durban and Coast Local Division)
[50] Financial Action Task Force 2017- International standards on combating money laundering and the financing of terrorism & proliferation – the FATF recommendations-updated 09.2017. //www.fatf-gafi.org/media/fatf/documents/recommendations/pdfs/FATF_Recommendations.pdf

attorney-client privilege in a criminal defense context only. Professionals such as accountants, auditors, lawyers, police and any other persons inclusive of company employees are expected to report any suspicious activities to the police under this law.

2.7 LOCAL COUNTER-MEASURES:

From an external perspective, one can contemplate a proactive role for auditors in the fight against money laundering. Considering the fact that auditors scrutinise client's books, the public expects them to be able to notice any irregularities in a client's business turnover. They regarded as first in line of defense against money laundering and reporting thereof.

Government Agencies are legally empowered to use following counter measures in attempts to combat money laundering schemes and accumulation it either illicit funds or illicitly attained properties:

2.7.1 Confiscation and Forfeiture

South Africa, like every jurisdiction has specific powers and limits to guide the confiscation of assets. The Confiscation and Forfeiture procedures permitted correspond with the legal traditions in the country. The South African criminal law encouraged forfeiture of assets acquired through criminal ways as a measure intended to restore the *ex ante* legal situation by depriving the offender from benefiting from illegal proceeds. The forfeiture regulatory regime allows for granting of a restraint order prohibiting any action by anyone in regard to suspected criminally acquired proceeds. POCA 121[51] regulates Confiscation and Forfeiture of any property that is suspect to have been acquired through criminal activities. This restraint is provided by Sections 25 and 26 of POCA 121[52] which provides for authorities to apply and be granted such a restraint order prior to or subsequent to a conviction.

This application can be brought on behalf of the state *ex parte* by the NDPP[53] (as empowered by Act 32 of 1998),[54] at any High Court. It is intended to preserve property by preventing any person from exercising any right over the property to which the restraint order has been issued.[55] This preservation of property provides for a recovery mechanism which in due course will be realised in satisfaction of a confiscation order.[56] The order is intended to capture benefits accrued through criminal ways by the defendant, regardless of whether he still has the illegally acquired proceeds. The South African confiscation and forfeiture law as contained in Proceeds of Crime Act 121 of 1998 (POCA) is modelled around the United States laws and the United Kingdom's *Criminal Justice Act.*[57]

2.7.2 The Audit Regulatory Body

The South African regulations regarding the regulators structure, its mandate and competence corresponds with the regulations in England, America, and other countries where various forms of oversight regulatory bodies were established. In the UK, regulatory bodies such as the FCA and NCA have robust powers to enforce Anti-Money Laundering regulations. They are also empowered to conduct investigations and imposing penalties for non-compliance, ranging from monetory fines to suspensions or criminal charges being pressed. Because of the recurrence of high level financial scandals, the alleged impairment of audit quality, and

[51] The Prevention of Organised Crime Act 121 of 1998
[52] The Prevention of Organised Crime Act 121 of 1998
[53] National Director of Public Prosecutions
[54] National Prosecuting Authority Act, 32 of 1998 (NPA Act).
[55] S 26(1) of POCA.
[56] *NDPP v Rautenbach* 2005 1 SACR 530 (SCA)
[57] *Untted Kingdom Criminal Justice Act,* 1998.

fraudulent misstatements, professional skepticism and auditor independence have received a great deal of attention from regulators globally (Glover & Prawitt 2014).[58]

In South Africa, the Auditing Profession Act No. 26 of 2005 (APA section 2 and section 3) used since the ACT governs the Audit Profession with the help of the Regulator's (IRBA) Code of Professional Conduct for Registered Auditors ("IRBA Code"). Auditors who perform the audit function in South Africa are expected to be registered with IRBA (as prescribed by The Auditing Profession Act 26 of 2005).[59] IRBA is a statutory regulating body that ensures that auditing firms and their registered employees deliver a high quality service that protects the financial interests of the public (Van Schalkwyk 2018:2).[60] This is a professional agency tasked with taking disciplinary action against auditors found to have gone truant.

The IRBA is jointly financed through the subscriptions, license and practice review fees of registered auditors and government funding (APA sect 25). The Minister of Finance, as a representative of the public interest, appoints competent people to the IRBA (APA sect 11(2)) for a period of two years (APA sect 12(1)), and the Minister is also responsible for monitoring and reviewing the regulator's performance (APA sect 28(2)). Various interested parties get to be also represented in the IRBA structure to counter the perception of self-regulation and protection of self-interests. According to sect 26 of the Auditing Profession Act, IRBA must report to the Minister of Finance about its performance in delivering its mandate against its strategic plan, submit its annual budget which covers a period of three years.

Section 4(1) (e) of the APA (2005) gives IRBA the mandate to prescribe audit professional standards. The Regulator is also responsible for registering and monitoring auditor's compliance with the law, as prescribed in section 45 of the FIC Act, read in tandem with the Act's Schedule 2. The IRBA has also incorporated the International Standards on Auditing (the "ISA's")[61] and other pronouncements as issued by the IAASB, IFAC's independent standard-setting body, in the rules to be applied by registered auditors in South Africa. These standards define auditing methodology and non-compliance can result in huge penalties and suspension for the auditor.

Armed with section 10(1)(a), read together with section 4 of the Auditing Profession Act, the IRBA is empowered to prescribe rules and standards for auditors professional competence, ethics and conduct. The Regulator has the statutory mandate to enforce these regulating standards and rules on auditing firms by ensuring that auditors adhere to these prescribed minimum standards of the profession.

Section 20(2)(f) of the Auditing Profession Act empowers IRBA to appoint a disciplinary committee to hear and determine charges of improper conduct against any registered person.[62]
Section 46(3)(a) of the Act refers to the auditor's negligence prior to or at the date the audit report is signed. Under this section Auditors who are unaware of their negligence do not have a legal duty to speak.

Subsequent amendments to the Auditing Profession Act governing the IRBA, gives the regulator powers to subpoena anyone with information required to complete an investigation. The regulator also has the power to enter, search and cease when conducting an investigating of auditors for improper conduct. The Act allows IRBA to recover the costs of an investigation

[58] Glover & Prawitt 2014; Knechel 2016; *The Economist* 2018a, 2018b
[59] SOUTH AFRICA. 2005. The Auditing Profession Act 26 of 2005. Pretoria: Government Printer.
[60] Van Schalkwyk, L. 2018. IRBA issues notice of transparency reporting for audit firms [Online]. https://www.irba.co.za (Accessed: 1 October 2018).
[61] (IRBA 2013 par 8 and IRBA 2013a)
[62] IRBA: https://www.irba.co.za/guidance-to-ras/disciplinary-process

from the inspected firm. These amendments were effected due to fact that the regulator experienced difficulties in gathering the evidence it required for its investigations.

The pitfall is that the IRBA inspection program is considered to be understaffed with inexperienced capacity considering its mandate, scope of authority, and number of required reviews. Some of these amendments to the laws are meant to rebuild public trust even though some provisions like search and seize orders do not sitting well with some audit firms. They claim that the amendments would affect not only auditors but third parties as well.

Of recently the Regulator (IRBA), has accused Auditors of lacking the requisite degree of independence and professional scepticism to prevent, detect and report on corrupt or negligent behavior of their clients (IRBA 2016; Maroun & Solomon 2014).[63] The regulator claimed that the auditors were failing societal expectations and this has resulted in public's loss of confidence in the professionals. Subsequently this has led to unwarranted litigation and Reputational Risks against Audit Firms.

Doubts about whether the Regulator is independent and acting in the best interest of the public have been raised occasionally, thus its independence in important cases has been questions especially where the public interest is involved. This is of prime importance since it can impact on the acceptability and credibility of the Regulator and the powers vested on it. Which then emphasizes the importance of appointing and involving various stake holders in the Board.

2.7.3 Policy Review

Due to the continued emergence of the financial scandals and fraudulent reporting, auditor independence and professional scepticism have received high level attention from regulators globally (Glover & Prawitt 2014[64]; Knechel 2016[65]; *The Economist* 2018a[66], 2018b[67]). The scandals have produced some disquiet among regulators, investors and the public at large about the adequacy of auditor independence.

Because auditors have been accused of being not independent and lacked professional scepticism required to prevent, detect and report on corrupt behaviour in companies, interested parties expected regulators to act promptly and apply stricter auditor regulations. In 2017 the IRBA issued mandatory audit firm rotation (MAFR) regulations, which were effective of April 2023, responding to allegations that auditor independence and scepticism was compromised and the results were production of reports with impaired audit quality. The intention was to reduce the length of audit firm tenures in line with Global best practice.

The issuing of theses mandatory rules caused considerable unhappiness in the audit industry. The majority of affected Professionals believed that existing regulations and codes of practice did not require amending. They believed that audit failures and scandals were not as a resultant of audit-firm long tenures, or from compromised independence and professional scepticism of auditors, but lack of stricter application of rules. Some ended up challenging the implementation of the rules in the Supreme Court of Appeal (SCA).

[63] Monroe, G.S. & Woodliff, D.R., 1994, 'Great expectations: Public perceptions of the auditor's role', International Journal of Auditing 4(8), 42–53. https://doi.org/10.1111/j.1835-2561.1994.tb00157.
[64] Glover, S.M.& Prawitt, D.F., 2014, 'Enhancing auditor professional skepticism: The professional skepticism continuum', *Current Issues in Auditing* 8(2), P1–P10. https://doi.org/10.2308/ciia-50895
[65] Knechel, W.R., 2016, 'Audit quality and regulation', *International Journal of Auditing* 20(3), 215–223. https://doi.org/10.1111/ijau.12077
[66] The Economist, 2018a, 'Reforming the Big Four – Shape up, not break up', *The Economist*, 24 May, viewed 24 June 2018, from https://www.economist.com/ leaders/2018/05/24/reforming-the-big-four.
[67] The Economist, 2018b, 'The great expectations gap. What is an audit for?'. *The Economist*, 26 May, viewed 24 June 2018, from https://www.economist.com/ finance-and-economics/2018/05/26/what-is-an-audit-for.

On 31 May 2023, in the SCA challenge case of *East Rand Member District of Chartered Accountants v Independent Regulatory Board for Auditors*,[68] IRBA received and accepted the Supreme Court of Appeal (SCA) judgement setting aside the Mandatory Audit Firm Rotation (MAFR) rules. The Judge ruled that the MAFR rules did not constitute a professional competency "standard" or a professional standard as prescribed by section 4 of the APA and therefore IRBA did not have the power to promulgate MAFR.[69]

This decision should not be confused with Section 92 of the Companies Act 71 which regulates and prohibits an "individual auditor" and "not audit firm" from serving a company for more than five years. Other countries like The US and UK went ahead and implemented the MAFR by initially addressing the ambiguities around MAFR by strategically targeting key risks and leveraged cooperation with other law enforcement agencies, both domestically and internationally.

2.8 GLOBAL COUNTER MEASURES:

It is a well-known fact that Money laundering is a spoiler when it comes to financial institutions' reputations and weakens relationships with investors, regulators and the general public. In 1989 the Group of Seven (G-7)[70] countries coordinated an international response to this danger and formed the Financial Action Task Force (FATF), a global money-laundering watchdog. Since the formation FATF membership has grown to over 30 countries and jurisdictions. The introduction of FATF has made the fight against illicit money to bleed into nearly every corner of the world through the tracking and freezing criminally acquired assets.[71]

But as many countries came up with ways to combat the many ways meant to conceal illicit proceeds, developing nations with their inadequate controls became an attractive alternative for launderers. These gaps have resulted in a significant and devastating impact on the security of these and other nations. This has hampered the growth of developing countries by discouraging foreign investors.

The use of Auditor's unique forensic skill could also be used to combat ML threats and expose any illegal proceeds derived through criminal schemes. In a classic case of the Bank of Commerce and Credit International (BCCI), the seventh largest private bank which was involved in the first highly publicized global money laundering operation, serves as a good example. The Bank had 400 branches in 72 countries and an estimated $20 billion in assets. Money launderers used drug money to buy BCCI certificates of deposit (CDs) in six countries that the Bank had branches in, and used certificates as collateral for loans. Their success was based on the fact that banking regulators did not have connections to monitor the inflow of money from other countries in which the bank did businesses.[72]

[68] East Rand Member District of Chartered Accountants v Independent Regulatory Board for Auditors (113/2022) [2023] ZASCA 81 (31 May 2023)

[69] *Op sit*

[70] G7 refers to Canada, France, Germany, Italy, Japan, the United Kingdom and the United States

[71] Nance, M. T. (2015). Naming and shaming in financial regulation: Explaining variation in the financial action task force on money laundering. In H. R. Friman (Ed.), *The politics of leverage in international relations: Name, shame and sanction* . New York: Palgrave Macmillan.

[72] Passas, N. I Cheat, Therefore I Exist: The BCCI Scandal in Context. In W.M. Hofman, J. Kamm, R.E. Frederick & E. Petry (Eds),International Perspectives on Business Ethics. New York: Quorum Books, 1993.

This scandal elevated money laundering crimes to the global agenda of the 1988 Annual Economic Summit of the G-7, subsequently issuing in 1990, 40 recommendations designed to combat corruption and related financial crimes. These were the first international AML standards and were used by governments as a basis to launch their respective AML plans and related regulatory regimes. Regardless of these developments, there's still a degree of apathy in investigating and reporting irregularities within the Auditing profession because auditors still feel that current measures and promulgated regulations to be ineffective.

In many instances auditors through educating their clients use deterrence to create awareness amongst their clients of the consequences of criminal actions, in the hope of inhibiting participation in any irregular activities that may be regarded as criminal. Auditors found to be negligent, dishonest, and colluding in fraudulent practices are also subjected to punishment in order to deter any recurrence of such.

Company internal controls are also used as a deterrence to inhibit employee fraud and misconduct. But when auditing firms and their employed auditors ignore auditing procedures including validating internal company controls, the chances are they also get implicated as being negligent. Unfortunately in many instances, culprits found guilty of being involved in these criminal offenses are often fined or sentenced to community service rather than been given harsher jail sentences since they are not deemed to be a threat to society. This leniency in punitive action is naïve and does less to deter the offenders from reoffending (Fredericks, McComas & Weatherby 2016).[73] In instances where the benefit from the crime outweighs the penalty, the deterrence becomes ineffective in combatting the crime committed.

The efforts by the South Africa government to investigate fraud and corruption has led to a number of investigative commissions been implemented. The most notable is the State Capture Commission (also known as the Zondo Commission of Inquiry) which on 21 August 2018, was launched to investigate allegations of state capture, corruption and fraud.

Two months after, on October 2018, another Commission of Inquiry was appointed to investigate the allegations of impropriety regarding the Public Investment Corporation (PIC). Its mandate was to investigate whether one of the directors had misused their position for personal benefit. Since then, the public still awaits to see punitive measures being handed out to the guilty parties from the recommendations of both inquiries. Which is proof that if the benefit of the crime outweighs the punishment, then deterrence has failed.

The potential benefits of these counter measures depend on the actual content of the legislated laws, the prescribed standards and their application in practice, and subsequent punitive measure in case found guilty. To take into Consideration the many scandals still emerging, one could easily argue that IFRS, the U.S. GAAP and other standards already passed are unable to serve the purpose.

2.9 THE AUDIT PROFESSION REGULATORY FRAMEWORK:

The Auditing Profession Act No. 26 of 2005[74] which is meant to govern the auditing profession, provides for establishment of an IRBA, protect the public interest, and develop and maintain

[73] Fredericks, K.A., McComas, R.E. & Weatherby, G.A. 2016. White Collar Crime: Recidivism, Deterrence, and Social Impact. Forensic Research & Criminology International Journal, 2(1):1-11.
[74] South Africa. 2005. Auditing Profession Act No. 26 of 2005:

internationally comparable ethical standards and measures meant to advance the implementation of professional standards and adherence to good ethics. The Act also provides for the education and training of registered auditors and candidate auditors. It provides for the accreditation of professional bodies and the registration and regulation of auditor conduct.

The Act was amended with the intension to strengthen the governance of the Regulatory Board, the investigation processes of the body including its disciplinary processes. The other intention was to provide powers for search, seize and subpoena people who might be privy to information required for investigation or disciplinary purposes by the Board. It was also amended with the intention to cover post investigation processes, provide for disciplinary process to be adhered to during the disciplinary inquiry and the related sanctions imposed, and to also provide for the protection and sharing of information. It also prescribed transitional measures to be considered after all these actions have been undertaken.

Section 37. (1) of the Act (APA) requires for an individual to use a prescribed application form to apply To IRBA to register as an auditor or a candidate auditor.

Section 41(6) (c) Prescribes that a registered auditor commits an offence for doing an audit in the absence of adequate risk management practices and procedures.

Section 44(1)(a) emphasizes the duty to report to the regulatory without delay by an auditor, if he suspects that a reportable irregularity has occurred or is taking place.

Section 44(1)(a) read with section 54(1) Requires that where a firm is appointed to perform an audit, that firm must immediately appoint responsible and accountable professionals to do that audit. The appointed auditors are expected to express an opinion about their respective client's fairness of their audited financial statements which were presented in line with International Financial Reporting Standards ("IFRS"). This requirement is aimed at enhancing the degree of confidence by intended users of the financial statements.

Section 44(2)(a) prevents a registered auditor to express an opinion in regard to any financial statement being a fair representation of the financial status of the entity and its operational cash flow, and that it has been properly prepared unless he is satisfied:

- That all assets and liabilities shown on the financial statements can be accounted for; (Section 44(3)(b))
- That proper accounting records have been kept; (Section 44(3)(c))
- That he obtained all information, vouchers and other documents required for the proper performance of his duties; (Section 44(3)(d))
- That he has complied with all laws relating to the audit of that entity; (Section 44(3)(f))

Section 45(1) of the Act (APA) imposes an obligation upon a registered auditor to report any anomalies.
Section 52(1)(a) prescribes non-reporting of financial irregularities by registered auditor as a crime.
Section 52(1)(b) prescribes that a registered auditor shall be guilty of an offense in case he recklessly expresses an opinion or falsify the audit statement.

2.10 CONCLUSION:
The commitment by the South Africa government to combat corruption and economic offences implies the existence of a political will, which can only be realised by providing the necessary skilled capacity and financial support. Then of course, government institutions would be able to implement the relevant legislations promulgated and supportive policies, processes and

procedures created with the intentions to manage, monitor and control prevalent conduct risks. The Government has noted that previous risk controls and compliance systems were not enough to resolve misconduct issues, thus promulgation of various legislation to reduce the risk. And yet still, there are gaps and regulatory shortcomings that have created serious corporate failures, resulting in mistrust by society about decisions made by auditors on big corporates.

In this Chapter the concept of Money Laundering and Money Laundering Control Legislation has been discussed in detail. Money movement and Laundering, Suspicious and unusual transactions and Counter-measures were discussed. A detail about money laundering control obligations by the South African government in line with global compliance was undertaken. We also discussed the Audit Profession Regulatory Framework in detail.

With all that done, the current legislative framework is still considered to be fragmented, inconsistent, and incomplete and seems not enough looking at the next chapter which will focus on how the Audit Firms got entangled with the Gupta Family and their Shenanigans.

Chapter 3: Audit Quality and the Audit Profession Ethics

3.1 INTRODUCTION:

The impact of the gaps and lapses that emerged during this period dented the trust and respect that the audit profession had enjoyed for decades, such that it called for serious changes to be engaged in order to save whatever is left of the audit professional reputation. It clear that South Africa has not been immune to similar scandals either, for example, the Gupta family company cases mentioned in the previous chapter, the Steinhoff case, the SARS rogue unit inquiry, and the VBS Bank debacle.

For decades the auditing profession has been regarded as one of the most noble and trustworthy professions, highly regarded globally by both investors and clients who relied on its credibility without any doubt. With the collapse of Enron in 2001, this trust in auditors started collapsing, and led to the downfall of Arthur Andersen as Enron's auditors. As a result of the Arthur Andersen collapse, the Big Five auditing firms became to be known as the Big Four. With the passing of time, a lot of industrialisation and a lot of service demand, small audit firms started to emerge, and a culture of dishonesty and negligent practices emerged too, resulting in breaches of independence, reputational damage, and loss of business and high turnover of experienced staff.

Moreover, there was an increase in incidents where auditors got threatened and coerced. In some instances their livelihoods were compromised. Sometimes they got enticed with money temptations. In the process the boundaries between being ethical and knowing what is ethical often got blurred and the quality of audit work got impacted upon.

In this chapter we will look at how issues such as auditor independence, how ethical behaviors and responsibilities of auditors can impact on the audit quality and tarnish the profession's reputation and the integrity of the firms they work for. We will also consider looking at factors such as professional skepticism that can effect irrational misconduct and unethical tendencies.

3.2 AUDIT QUALITY:

Audit quality is difficult to define and measure, however defined in simple terms it refers to the probability that an auditor that is auditing a client will uncover irregularities that are in breach of the law, and on discovery, will report them to the legal authorities. In order to achieve this, the auditor's independency off the client, his competent and capable behaviour is of utmost necessity throughout the auditing process in order to produce an appropriately high-quality audit that enhance user confidence in audited financial statements (Knechel 2016).[75] The concept of audit quality is very important to auditing research, especially when assessing the impact of regulatory regimes (Hay 2015).[76]

DeAngelo (1981:186) [77] simplifies the definition of audit quality as the probability by auditors to detect issues that are particularly financial in nature and are noncompliant with legal requirements, and subsequently report such breaches to the appropriate authorities.

But then one must also understand that audit are not meant as a guarantee that fraud will be detected, because it entails sophisticated procedures aimed at concealment. The fact of the matter is that the most harmful financial fraud is not easy to detect, no matter whether the audit

[75] Knechel, W.R., 2016, 'Audit quality and regulation', *International Journal of Auditing* 20(3), 215–223. https://doi.org/10.1111/ijau.12077
[76] Hay, D., 2015, 'The frontiers of auditing research', *Meditari Accountancy Research* 23(2), 158–174. https://doi.org/10.1108/MEDAR-12-2014-0062
[77] DeAngelo, L.E., 1981, 'Auditor size and audit quality', *Journal of Accounting and Economics* 3(3), 183–199.

was conducted with due care and in compliance with auditing standards. The detection of fraud is not dependent on the knowledge and experience of the auditor but on facts such as the perpetrator's expertise, his power and influence, and the frequency of commission of the act.

The Companies Act 71 of 2008, and APA's[78] Section 44 (2), both emphasizes the fact that the primary duty of an auditor is to examine and audit the annual financial statements of their client and the two Acts relate on how this duty is to be performed which will enhance the chances of detecting fraud if the "how" of it is fully complied with.

Lack of auditor scepticism was clearly observed in the Eskom deal that was signed for a period of two years for a new, R3.6 billion consulting contract for a capital scrubbing project with PwC, a professional services company with revenue of $37.7-billion. In return PwC was coerced by Eskom Management, to choose Nkonki, a very small local player in the accounting and auditing industry as their supplier development partner. Nkonki had just been bought by the Gupta family through a management buy-out financed from the Gupta Family coffers. Nkonki made R1.1-billion out of the contract, and the Gupta family got 65% of Nkonki's profits.[79]

The PwC relationship with Nkonki was not the only one forced, there were other relations that were strategically forced between Gupta companies and auditing companies, such as that between the German IT giant SAP, and Global Softech Solutions, a Gupta owned IT Company joined as a supplier development partner on an R800-million Transnet contract. The Guptas claim that these imposed relations were all pure coincidence, whilst auditing companies claim ignorance of the fact that the companies they were partnering with were linked to the Gupta family. In all these Auditor-Gupta company relations, PwC exonerated itself from the obligation to identify fraudulent transactions. Whilst public outcry was that it is its lack of scepticism which either resulted in failure to detect problems early, or a failure to act on a problem recognised, considering their proximity to these companies and the link to Gupta family.

This link between professional scepticism and audit quality is an extremely important factor that forces auditors to identify and investigate potential irregularities and misstatements. It is therefore required of auditors to act with professional' scepticism that requires due diligence and a standard of care, observing, probing and questioning all information that they exposed to before making any opinions. Lack of such independence can result in a risk of not getting qualitative or quantitative auditory evidence to be used by auditors in forming an opinion. It is therefore important to be sceptical and independent, and appear as such to outside parties. It is also important to ensure audit quality and to provide the necessary reassurance to users of audited financial statements.

3.3 FACTORS AFFECTING AUDITING QUALITY:

The following factors were found to can affect Audit Quality:

3.3.1 Auditor's Competence: The introduction of professional standards in line with international best practice by IRBA was one greatest achievement in developing and claiming trust for the audit profession. Professional standards define the profession's body of theory and forms the profession's basis in terms of which its members can rationalize their functioning. This professionalism entails control by a statutorily regulator over professionals to prevent abuse of their professional powers and ensure the "homogeneity of service" of individual members. Regulators are meant to establish and enforce compliance with

[78] South Africa. 2005. Auditing Profession Act No. 26 of 2005. Cape Town: Government Printer

[79] AmaBhungane, Eskom's new billion-rand consulting deal for Essa & Co (The daily Maveric: The Nkonki Pact Part 2.29 March 2018)

professional standards of practice in order to facilitate homogeneity of service of their registered members.

It is easy for an auditor who is competent, to identify gaps in the management system processes and recommend to the management team on areas that require improvement. Such an auditor requires simple core competence and Skills such as communication skills that are inclusive of oral, written, report writing, presentation skills including but not limited to problem identification and solving, solution skills such as conceptual and analytical thinking, and many new skills identified to be relevant to the profession. It is necessary of professionals to keep up to date with their industry's professional standards and regulatory changes.

3.3.2 Auditor's Integrity: This principle requires auditors to be direct and honest in their professional relationships. It requires them to deal with their clients in a fair, truthful and honest manner in all relationships. This principled expectation requires that professionals not to associate themselves with reports that contain misinformation, or materially false or misleading statements that omits or obscures important information required by the client or investors and any interested party.

A classic case of such drop in integrity is that of Steinhoff South Africa. Media reports in 2017 alleged that Steinhoff was involved in accounting irregularities.[80] The allegations were in relation to Steinhoff's management inflating its earnings and concealing losses.[81] This scandal resulted in the company's shares immensely dropping in value and the CEO of the company's resigning. Steinhoff CEO faced a barrage of charges such as fraud, racketeering, and contravention of the FMA (Act 19 of 2012) at the Specialised Commercial Crimes Court in South Africa.

Steinhoff South Africa auditors, Deloitte, were investigated and disciplinary action being taken by the IRBA, the regulating authority, for the work that they did on Steinhoff's financial statements for the years 2014, 2015 and 2016. The IRBA found that there was collaborative wrongdoing by Steinhoff's directors, the fund managers, and their auditors in that they created an enabling environment conducive to money laundering.

3.3.3 Auditor's Objectivity:

The Objectivity principle imposes an obligation on all auditors not to compromise their professional judgment because of bias, conflict of interest or the undue influence by their clients. The principle requires their professional diligence and compliance with applicable standards at all times even when exposed to situations that may impair their objectivity.

The Auditors are required to avoid relationships that are threatening in nature, or bias or unduly influencing their professional judgment. Such threats to auditor principle-compliance might be created by a broad range of facts and circumstances that cannot be easily defined. Because of the difference in the nature of engagements and work assignments, it might be required that one employs different types of approaches. Should the auditor feel that his or her objectivity might be compromised, they should divorce themselves from such a contract.

[80] Mchunu, S. 2018. Steinhoff Scandal Cost Government Employees Fund R20bn. *IOL*: 1–2. https://www.iol.co.za/business-report/companies/steinhoff-scandal-cost-government-employees-fund-r20bn-13041991 12 December 2018.

[81] Kew, J. & Bowker, J. 2018. We're Not Friends - Steinhoff Ex-CFO Blames Jooste, Auditors for Accounting Scandal. *Fin24*: 1–4. https://www.fin24.com/Companies/Retail/were-not-friends-steinhoff-ex-cfo-blames-jooste-auditors-for-accounting-scandal-20180829 12 December 2018.

3.3.4 Auditor's Accountability:

Financial accountability has become increasingly essential for any organization nowadays in order to preserve faith in the integrity of corporate financial reports. One means of effecting accountability is through auditing ones performance or actions. Without accountability people fail to take ownership of their actions, because they don't believe they will be subjected to any consequences.

To be accountable in rendering their services Auditors need to be knowledgeable and careful in their professional practices. In accepting to audit a client's financial statements renders an auditor legally liable and responsible for any misstatements or instances of fraud that can rise from the statements. This fact compels Auditing Firms to prevent a high turnover of their knowledgeable auditors because it can easily preclude intimate knowledge about the industry they auditing. Also any act of negligence by newly appointed auditors can cause them to be legally liable.

This stance has made Auditing very competitive thus encouraging avoidance of shortcuts. There's a need to caution Audit Firms to refrain from compromising Auditing Standards out of Fear of Losing a Client, or effect some cutbacks in auditing work because of the pressure that auditing fees had placed on audit firms.

3.3.5 Auditor's Confidentiality: The Confidentiality principle requires an auditor to keep secret the information acquired as a result of professional service rendered. He is also required not disclose the client's confidential business information without the client's consent, unless bound by a legal duty to disclose such information. It also prevents the auditors from using for the personal advantage such acquired information.

The need to maintain confidentiality of information at all times and be sensitive and avoid inadvertent disclosure of such information to associates, immediate family or work colleagues should be avoided at all times is a need that an auditor should consider at all times. The need to comply continues even after the contract with the client has come to an end.

Disclosure of irregular information is the only legally permissible disclosure known, and should be authorised by the client during contracting. To decide whether to disclose or not, factors such as whether the affected party's interests could be harmed if the client gives his permission to disclose or not should be considered by the auditor.

3.3.6 Auditor negligence: Auditors have a duty to exercise due care and diligence while discharging their duties, anything contrary to this may be construed to be negligent. Auditor negligence refers to failure to properly review the company's accounting records and systems, failing to identify and report material misstatements in the said financial statements, and failing to comply with auditing standards. This failure can damage the company's reputation and erode shareholder confidence.

The role played by auditors in ensuring the financial health and transparency of companies is very crucial, yet sometimes they may fail to discharge their duties industriously, leading to negligence. This may result in issuing an unqualified audit opinion despite knowing of material misstatements in the financial statements. This can lead to investors making uninformed investment decisions, and if an auditor is found to have been negligent, they may be held liable for damages. It is also important to note that materiality is a financial reporting concept, rather

than an auditing one. To consider the existence of negligence, one needs to consider the foreseeability of harm and whether steps could have been taken to guard against the loss.[82] Failures such as negligent behavior have created corporate crises that have had far-reaching consequences, such as obliterating employee benefits like pensions. The Steinhoff International scandal is a clear case-example of this, its share price crashed by 90% in 2017 after the news broke about the company's financials being scrutinised for "accounting irregularities requiring further investigation."[83]

The CEO of Steinhoff International, Marcus Jooste upended two major fraud cases against him in South Africa and Germany. The investigations established that he had too much influence over the auditors thus influencing them to overlook certain matters that resulted in material misstatement of the company financials statements.

He was found guilty in South Africa for publishing false and misleading annual financial statements and annual reports for 2014 to 2016 and for the 2017 half-year about Steinhoff entities. He was fined R475 millions, and he committed suicide 2 days after the verdict.

3.3.7 Conflict of interest: A professional accountant is always obliged to comply with the fundamental principles of his profession. Independence in auditing ethics refers to the impartiality and autonomy of auditors in conducting their work. It involves the absence of any incentives, influences, or relationships that could compromise the auditor's objectivity and professional judgment.

There may be times, however, that compliance with fundamental principles will be explicitly or implicitly threatened by the client or any interested party. Non-compliance with professional standards can also exist in instances where the auditor attempts to satisfy his client's profitability interests and costs cutting objectives. By so doing, the compliance levels are compromised and auditors get to keep their jobs. When faced with such pressures the auditor is expected to take necessary corrective measures to eliminate the threats and reduce threats to an acceptable level.

The audit firms do not only do auditing services for their clients. They also provide tax advisory and consulting services, financial and risk management services for the clients. At times provision of these services can pose potential conflicts of interest because of income that the firms make in providing these services even though highly regulated. The risk presented in some instances is that some firms will prefer to avoid "rocking the boat" with their valuable client who uses more than one of their services either as internal and external services provision and pays lucrative fees to the firm. In such instances, many audit firms fail their legal obligations in terms of reporting any suspect irregularities.

This risk result in some of the audit firms getting to use the knowledge they acquired through other services they offered to their clients to assist them to avoid paying tax and thus enabling illicit flow of funds. This serves as evidence that sometimes auditors do cross the line and become complicit in establishing structures that promote criminal behaviour. Such behaviour by auditors is subject to discipline by IRBA and can also be subject to criminal litigation.

[82] Cape Empowerment Trust Limited v Fisher Hoffman Sithole 2013 5 SA 183 (SCA) Maya, Cachalia, Shongwe JJA and Swain AJA concurring.

[83] Ann Crotty,"Deloitte in spotlight again with African Bank hearing" *Bussiness Day* (Johannesburg 19 March 2018) https://www.businesslive.co.za/bd/companies/financial-services/2018-03-19-deloitte-in-spotlight-again-with-african-bank-hearing/

The involvement of KPMG and McKinsey in the Transnet locomotives tender is one classic case of conflict of interest. The tender was divided between the four train manufacturers (Faull et al. 2014),[84] Bombardier, General Electric, CSR and China North Rail which was represented by the Guptas and Duduzane Zuma (Jacob Zuma's son) (Bhorat et al).[85] The National Union of Metalworkers of South Africa (NUMSA) raised a complaint with the Public Protector about the involvement of the Gupta Family. Their complaint was around concerns of patronage and conflict of interest. They claimed "that the contracts were used to line the pockets of a selected minority business and political elite." (NUMSA, 2015:2).[86]

These concerns were corroborated by the fact that Iqbal Sharma, a political appointee to the Transnet Board, was alleged to be a Gupta family associate and oversaw the awarding of the tender (Bhorat et al. 2017). During the time that Sharma was overseeing the locomotive tender at Transnet, he was shareholders with Duduzane Zuma in one of the Gupta companies. This disregard of independence and conflict of interest by him raised a lot of questions which KPMG seemed to overlook. Another Gupta company that benefited from the locomotives' tender was Trillian Asset Management (Bhorat et al., 2017:28). The company was appointed as Transnet advisors on the financial arrangement and corporate structuring of the locomotive deal whilst McKinsey was the auditing company.

A South African Treasury investigation report[87] on state capture revealed that McKinsey paid for Anoj Singh, then CFO at Transnet, to go on holiday to Dubai, UK, Russia and Germany, after he renewed their contract with Transnet worth R3.1 billion as an advisory firm. This follows the findings of Fundudzi Forensic Services investigations[88] on behalf of National Treasury into Eskom, Transnet, McKinsey and others. This report investigated the procurement of the 1,064 locomotives from China South Rail and China North Rail with costs inflated by R1.2bn and R16bn respectively.

The report further claims that McKinsey also facilitated and paid for Singh's eight-day trip to Dubai, and secured his visas and accommodation at London's Langham five-star hotel when he attended the CFOs conference in London, as well as his transit accommodation at the Sheraton Frankfurt Airport Hotel. Singh attended the CFO conference the following year via Moscow and Dubai at McKinsey's cost again. This relationship between McKinsey's and Trillian extended to Eskom operations as Singh became Eskom's CFO and the corruption game continued.

The investigation also established that McKinsey influenced Singh to convince Popo Molefe (Chairperson of Transnet) to appoint them to help renegotiate Transnet locomotive tariffs contract, thus compromising the integrity of the procurement process. Subsequently McKinsey was given preferential treatment and got appointed even though their tender proposal was late. According to the report Transnet, in total paid McKinsey R1 993 trillion between 2005 and

[84] Faull, L., Bhardwaj, V. & Letsoalo, M. 2014. Transnet Tender Boss's R50-Billion Double Game. *Mail & Guardian*: 1–7. https://mg.co.za/article/2014-07-03-transnet-tender-bosss-r50-billion-double-game 12 February 2018.

[85] Bhorat, H., Buthelezi, M. & Chipkin, I. 2017. *Betrayal of the Promise: How South Africa is Being Stolen*. Cape Town. http://pari.org.za/wp-content/uploads/2017/05/Betrayal-of-the-Promise-25052017.pdf.

[86] NUMSA. 2015. Statement by Numsa and Labour Unions to Strike Against Corruption on 30 September 2015. *www.numsa.org.za*: 1–6. https://www.numsa.org.za/article/statement-by-numsa-and-labour-unions-to-strike-against-corruption-on-30-september-2015/ 12 February 2018.

[87] Nicki Gules And Sipho Masondo, "Treasury drops looting bomb" *News24* (Johannesburg, 29 July 2018) https://www.news24.com/SouthAfrica/News/treasury-drops-looting-bomb-20180729-4

[88] Nico Gous, "Transnet paid McKinsey, Trillian and Regiments more than R3bn" Timeslive. (Johannesburg 16 November 2018) https://www.timeslive.co.za/news/south-africa/2018-11-16-transnet-paid-mckinsey-trillian-and-regiments-more-than-r3bn/

2016. The investigative report further recommended that former Transnet executives, as well as Trillian's Daniel Roy and Johannes Faure be criminally investigated and charged for the above discussed irregularities.[89]

3.4 AUDITOR'S ETHICAL RESPONSIBILITIES:

The importance of ethical considerations within the auditing profession has taken a positive center stage in response to a public demand about professional accountability, especially in the aftermath of audit failures happening both locally and internationally. The failures have impacted negatively on the audit profession as a whole and prompted IRBA to issue ethical standards and guidance on audit services as key to sustaining a profession and creating common values for the audit profession. Mandated by Section 4(1) (e) of the APA, the IRBA can prescribe and/or adopt International Standards on auditing (IRBA 2013 par 8).[90] In terms of Section 47 of the APA,[91] IRBA is mandated to oversee execution auditors' duties and ensure that auditing firms adhere to prescribed minimum standards of the profession. These standards are regarded as a detailed guidance on audit methodology, and non-compliance with them can result in disciplinary action been taken against the audit professionals or their employing firm.

The importance of these ethical standards to a firm's reputation and public trust, including the promotion of professional ethics and improvement of firm's governance systems, becomes a hefty challenge in the existence of conditions that are a threat to compliance with fundamental auditing principles. In instances whereby the auditor is contractually bound and obliged by client to detect fraud, the auditor will have a legal duty to detect such fraud as is contracted. This becomes one of the ethically challenging situations to the value of auditor independence. If the auditor fails to perform his contractual duty, he can only plead impossibility of performance, so long as he can prove that the obligation would unduly and cumbersomely burden him. To minimize such incidents, audit clients are advised to desist from deliberately misleading auditors.

In evaluating the level of threats to auditor compliance, relevant factors such as the auditor's educational training and experience be clarified from the start, the existence of conducive conditions for the audit to happen independent of influences, and the clarity on issues that are binding the auditor to test and report on specific regulatory noncompliance issues to be include in the Liability Limitation Agreement (LLA). Proper supportive policies and procedures around corporate governance, effective complaint systems, and professional or regulatory monitoring and disciplinary procedures, might also be a necessary.

As an example one can refer to the gradual decline in credibility case study of KPMG in South Africa, which is something that took many years. KPMG was fast growing with outsized political influence and alignment in a period of 15 years. In that period they had 30 of the Gupta companies such as Linkway and Oakbay as their important clients. Then came the "#Guptaleaks,"[92] internal emails leaked from their companies implicating KPMG's to allegations of being accessory to illicit money transfers and a political campaign to defame ministers. This resulted in KPMG's sudden death. It was alleged that the Auditing Firm helped the Gupta's structure their Dubai-based precious-metal firm, for tax evasion purposes.

[89] *Supra*
[90] Institute of Internal Auditors (IIA), The. 2010. International standards for the professional practice of internal auditing. Alamonte Springs, FL: IIA.
[91] South Africa. 2005. Auditing Profession Act No. 26 of 2005. Cape Town: Government Printer
[92] AmaBhungane and Scorpio, "The #GuptaLeaks" Daily Maverick (Johannesburg, 27 November 2017)

It was further alleged that they helped the family fraudulently divert funds from a dairy farm project to a Gupta company so that the funds can be used for payment of hotel accommodation for the family wedding, thereby colluding with the Gupta family to evade paying taxes on the funds (Daily Maverick: 1–3, Maimane, 2017:1).[93] The media accused them of being "efficient enablers" of illicit financial flows against the country laws and thus needed to be penalised.

KPMG denied the allegations of facilitating any corruption, yet all these irregularities were glaring in their face and they failed to report the suspicions as is required by law. What followed next was a forced public apology and a management change for the South African operations. Too many questions remained unanswered by the Audit Firm, such as: How could the firm not pick up such straight forward money laundering schemes? What exactly were they auditing if they could not pickup such anomalies? Their ethical existence and credibility were being put to question.

3.5 CONCLUSION:

The Gupta family businesses became the center of alleged corruption and money laundering scandals that had put international firms like KPMG, McKinsey, SAP and PwC into reputational discredit. The Audit profession suffered a trust deficit because of featuring prominently in these scandalous many events**.**

With these problems in mind, the majority of scholars today argue that auditors are not obliged to detect fraud or errors during auditing, more so if there are no circumstances that raise suspicions. The mere existence of fraud or errors in a client's financial statements should not result in this duty either. But others argue that due diligence and professional care must be undertaken to prevent any burdensome outcomes. Once fraud is detected and revealed, it becomes easy to connect it to its earlier manifestations and if material irregularities appear, it becomes the auditor's duty to raise alarms and report to respective authorities.

The auditor's conduct on such matters must be examined in such a way as it came to him at the time when he had an unsuspicious mind. A careful auditor is reasonably expected to revisit past evidence to bring to mind current and past irregularities, and therefore is expected to remember and consider other irregularities, especially those occurring in a connected way.

When an auditor identifies a threat to compliance that may possibly result in him being implicated with misleading information, the auditor must evaluate the level of such a threat and consider whether it is at acceptable level. One is expected to use the "reasonable and informed third party test" to conclude as to whether the auditor is still complying with the fundamental audit principles. If after evaluation it is found to be impossible to reduce the threat to an acceptable level, the auditor should refuse the task and dissociate with the misleading suspect information, and should consider reporting the misinformation as required In terms of The Auditing Profession Act 2005 (APA).

[93] Maimane, M. 2017. Estina Dairy Farm: A Corruption Crime Scene in Vrede. Daily Maverick: 1–3. https://www.dailymaverick.co.za/opinionista/2017-07-18-estinadairy-farm-a-corruption-crime-scene-in-vrede/#.WuTWjYiFOCg 28 April 2018.

Chapter 4. The Gupta family and the involvement of auditing firms

4.1 INTRODUCTION:

The emergence of South African scandals are instrumental in the generation of a lot of illicit proceeds and this undermined the efforts by enforcement agencies in their attempts to combat these criminal activities. The auditing profession is also severely affected by this wide-spread corruption and unethical behavior. The involvement of the big auditing firms in allowing the Gupta Family to milk the South African economy millions of Rands has become a sore point not only to the nation but to the international world.

In this chapter we will introduce the various case studies relating to South Africa, the alleged irregularity incidents and auditing firms implicated in negligent and dishonest practices. We will also give a brief introduction about the Gupta family, their companies involved, and engage the reaction of the Government and Business to these allegations.

The objectives of this chapter are to improve one's understanding of the value of auditor independence and ethical behavior to an Auditing firm's reputation. To understand how professional skepticism can impact irrational misconduct and create ways to improve professional's ethical trust. The chapter will introduce the Gupta family and their link to the Auditing firms, and how they managed to siphon million out of state owned entities, and Governments reaction to these irregularities.

4.2 GUPTA FAMILY EMERGENCE AND CONDUCT:

Gupta family originally came from India to South Africa in the 1990s just as apartheid was coming to an end. With a startup of selling shoes they built a multibillion Rands business empire of more than 30 Gupta companies in South Africa. With that much money to amass and their relationship with President Jacob Zuma, they embarked on plan to plunge the country into a political crisis that led to the establishment of a State Capture Commission.

Their family businesses became the center of alleged corruption and money laundering scandals that had put international firms like KPMG, McKinsey, SAP and PwC into reputational discredit and led to the resignation of the then South African president Jacob Zuma. The family had been at the center of the state capture allegations by being proxy to then President and his son, Duduzane Zuma.[94]

The assumption has been that, one could only do business in South Africa by going through the Gupta family. It looked like all firms were forced to first declare their interests to the Guptas and their associates before getting tenders. Big firms like McKinsey & Company, got largest contracts in Africa, by partnering with a Gupta company on one of their scandalous deals that saw money being ultimately channeled through to a Gupta-linked firms based in Dubai. They used companies like Bell Pottinger, a public relations firm based in London to create fake-news on web sites to inflame racial tensions and badmouth their vocal critics in South Africa. For a pay, the PR Company spread propaganda about a "white monopoly capital" that was targeting the Guptas with ulterior intentions to recreate "economic apartheid." The company was paid through Oakbay Investments, another Gupta company. They terminated their PR contract with the Guptas in April 2017 as public acrimony about services to the corrupt Guptas increased, citing abusive and threatening comments against its public relations staff. Its operations collapsed globally as some of its clients withdrew their business.[95]

The Guptas also used KPMG at a price of $1.65 million to discredit SARS and its tax officials who were investigating them. The officials were portrayed as a "rogue unit" that is alleged to

[94] Bhorat, Haroon et al (2017), Betrayal of the promise: how South Africa is being stolen, Report by the State Capacity Research Project (EST, PARI, DPRU).

[95] ANCIR, "Inside the #GuptaFakeNewsEmpire: The Guptas, Bell Pottinger and the fake news propaganda machine" *Times Live* (Johannesburg,04 September 2017)

have engaged the services of prostitutes during their leisure time by the audit firm, and that the unit was spying on the Zuma. The fake-news led to several senior SARS officials being forced to resign or face being fired, many chose to resign.

By being close to President Zuma, and being helped by leading Auditing international firms like KPMG, McKinsey, SAP and Bell Pottinger, the Gupta family managed to milk the South African Government about $7 billion. President Zuma, their ally, was forced to resign, McKinsey apologised publicly for their role in these high level scandals. The Gupta brothers avoided prosecution by fleeing the country to Dubai. Their Optimum coal mine, which the family had obtained in a deal brokered and financed by government money, declared bankruptcy.

Their company's activities drew the attention of the former Public Protector, Thuli Madonsela, who outlined in detail In a 355 pages report just how much control the Gupta family had over government resources with the help of former president Jacob Zuma. The report offers proof of how state companies were defrauded and used for personal enrichment and money laundering.[96] Both the Guptas and Zumas have denied any wrongdoing.

One of the State owned Companies (SoE), Eskom is mentioned 916 times in the report. The report alleges that Eskom prepaid one of the Gupta companies, Tegeta Exploration and Resources, R600 million in an attempt to help to finance the Guptas' coal mine deal to supply Arnot Power Station through its preferential treatment policy. The report alleges that this transaction was done for the sole purpose of funding and enabling Tegeta to purchase all shares in Optimum Coal Holdings and thus control the coal supply chain to Eskom.[97]

The mounting public pressure based on media revelations that Gupta family had looted the Estina dairy project in the Free State, forced the Asset Forfeiture Unit to seek a preservation order of R250m at the high court in Bloemfontein which was granted. And the South African National Prosecuting Authority on the other side awaits a decision by the United Arab Emirates government to grant them a preservation request of about R169m that the Gupta family laundered out of South Africa.

Subsequent to the public protector's report came about the release of the "#GuptaLeaks",[98] an email dossier by investigative journalists which bolstered longstanding allegations of corruption at state owned companies like Eskom, Telkom and Transnet. The finance minister started to question some of the lucrative tenders given to the Gupta-controlled companies by state owned companies. The government instituted a commission of enquiry against the Guptas and their alleged state capture tendencies.

4.3 THE CONDUCT OF AUDITING FIRMS IN GUPTA LINKED BUSINESS:

Local news media, through their investigative journalism reports of a trove of leaked emails, indicated how the Guptas allegedly abused their relationship with Zuma and ministers to profit from government tenders. And how big auditing firms like KPMG were manipulated to audit transactions suspect of money being laundered in and out of South Africa.[99]

The release of the leaked emails used by local news organisations to report on how the Gupta family abused their relationship with Jacob Zuma, bolstered the longstanding allegations of corruption in Eskom and Transnet which are State owned Companies. Both companies were

[96] Public Protector South Africa, *State Capture Report* (Report No:6 2016/2017) https://cdn.24.co.za/files/Cms/General/d/4666/3f63a8b78d2b495d88f10ed060997f76.pdf.
[97] op cit
[98] AmaBhungane and Scorpio, "The #GuptaLeaks" *Daily Maverick* (Johannesburg, 27 November 2017)
[99] op cit

involved in controversies under the watchful eye of credible auditing firms.[100] We are to detail how these Audit companies were involved, overlooking compliance and ethical values.

4.3.1 KPMG

The accusations meted out to KPMG South Africa for facilitating tax evasion crimes by the Gupta family, as well as the Firm's role in investigating and pronouncing the alleged SARS rogue unit (Shoaib, 2017:1; 2018:3; Cameron, 2017:1; Quintal, 2017:1), and the investigation about the work they did for VBS Bank literary put KPMG on a global spotlight. Investigators alleged that KPMG assisted the Gupta's to pay for a lavish family wedding in South Africa by laundering R30-million from a government funded dairy project. Over and above, KPMG SA CEO, Moses Kgosana was invited to attend the same controversial wedding, which invitation he subsequently accepted and when media started to expose the scandal, he resigned from KPMG under public pressure.

The wedding expenses were falsified as business expenses deductible for tax purposes (Wild, 2017:1),[101] and Section 23 of the Income Tax Act 58 of 1962, prohibits such classification of expenses as business expenses. It can therefore not be argued that KPMG was not aware of how these expenses were treated (Khumalo, 2017)[102], yet they failed to act on them in terms of the law[103], resulting in the allegation that KPMG was accessory in helping Linkway Trading to evade tax.

On the face of these allegations and media pressure, KPMG concluded that it fell short of its own standards during the 15 years it audited Gupta firms, and subsequently expelled its remaining top management in SA.[104] The IRBA and SA Parliament were also vocal in condemning KPMG's ignorance after it was established that KPMG allowed Linkway to register a wedding as a business expense, avoiding to pay tax at the expense of the Free State's Provincial government's generous donation.[105] How generous was this donation? It is alleged that one so called Minister Zwane, who by then was a Free State MEC for agriculture, used his influence to ensure that Estina is given a free 99-year lease to a 4,400-hectare farm in Free State. Furthermore, he ensured that the Provincial Government invested R114m into the non-existent 'dairy project' run by this company.[106]

It is alleged that Estina then transferred US$1 999 975 of its loaned R114millions to a Gupta owned company, Gateway Limited in Dubai. Gateway immediately transferred US$1 600 000 of that amount to yet another Gupta UAE company, Global Corporation LLC. After this transfer, Global Corp LLC transferred US$1 590 000 and $10 000 in two separate transactions to Accurate, another Gupta company which was invoiced the US $10 000 for the Sun City wedding by Linkway, another Gupta company organising the wedding. After these transfers were done Gateway added $25 to its balance to round it to US$400 000 and then transferred it to Accurate's account. In simple terms, though it might look confusing, meant that the Gupta's had the US$1 999 975 government's cash transferred by Estina to Gateway.

KPMG, as auditors of Linkway Trading Ltd, literary failed to question the origin of the wedding funds. Its subsequent self-instituted internal review process found no wrongdoing by its staff or the firm. Yet it is clear that during the 2014 audit, the firm amended Linkway's financial

[100] AmaBhungane and Scorpio *op sit.*
[101] Wild, F. 2017. KPMG Watched as Guptas Moved South Africa Public Funds for Wedding. *Bloomberg*: 1–3. https://www.bloomberg.com/news/articles/2017-06-30/kpmg-watched-as-guptas-moved-s-africa-public-funds-for-wedding 28 April 2018.
[102] Khumalo, K. 2017. Board for Auditors Claims Evasion by KPMG. *IOL*: 1–7. https://www.iol.co.za/business-report/board-for-auditors-claims-evasion-by-kpmg-11476809 30 April 2018.
[103] Section 45 of the Audit Profession Act (Act 26 of 2005),
[104] Hosken, G. "Named: KPMG executives axed over Gupta scandal" *Times Live* (Johannesburg,15 September 2017)
[105] Hosken, G. 2017b. KPMG Ignored Red Flags. *Sunday Times*: 1–4. https://www.timeslive.co.za/news/south-africa/2017-09-15-kpmg-ignored-red-flags/ 20 October 2017.
[106] Kyle Cowan, "Estina: From R9k to R34-million in one day - and how the Guptas stole it" *Times Live* (Johannesburg 22 January 2018) https://www.timeslive.co.za/news/2018-01-22-estina-how-the-guptas-stole-millions/

statements with the intention to move R6.9m which was used to settle the hotel bill for lavish wedding guests. From a reasonable man's principle, the firm could not claim no knowledge of these accounting irregularities, and did not report as is required by Section 45 of the Audit Profession Act (Act 26 of 2005) (APA).[107] This emphasized the allegation of tax evasion by Linkway Trading with the assistance of KPMG. In light of further revelations and pressure from the media, KPMG expelled its top management in the country after concluding and accepting that it fell short of its own standards. Even though it was glaring that KPMG had intentionally misrepresented facts and that Linkway's tax was reduced unjustifiably. [108]

Although KPMG immediately terminated its contracts with the Gupta companies after these revelations, IRBA conducted a multi-faceted investigation into KPMG audit work it did for Gupta family-owned businesses beyond the initial investigation into the audits of Linkway Trading, including its report on the SARS "rogue unit", and the subsequent compliance problems at VBS Mutual Bank, which was subsequently placed under curatorship and a forensic investigation undertaken, and the Bank closed shop.

With all this mounting pressure on the Firm, KPMG offered to refund the R23 million fee it received from SARS for their services, it furthermore donated R40 million to charity of their choice. This after an internal investigation by KPMG International on audits done for the Guptas and the 2014/15 report on SARS's alleged rogue unit. Its involvement in SARS had destabilized the South African Ministry of Finance, in that it implicated the Finance Minister in person and compromised SARS, resulting in high staff resignations after that expose.

KPMG took 18 months of denials to withdraw its "rogue unit" report and issue a qualified public apology for their actions. In response, SARS announced their intended right to sue KPMG for the withdrawal of the "rogue unit" report without consultation them first. They further indicated that would seek to have the company's license to operate in South Africa withdrawn.

As if that was not enough for KPMG, the investigations extended to the work they did VBS Bank. It was discovered that nearly R1 billion was unaccounted for among other dodgy dealings at the Bank. VBS's internal auditor PwC denied complicity from the bank financial mess, claiming that its role was focused on the bank's governance processes, its risk management systems and its internal control systems. PwC somehow exonerated itself from the obligation to identify fraudulent transactions.[109]

This saga at VBS brought back the beleaguered KPMG into the spotlight again, when two senior partners at the firm who were lead audit partners on VBS, resigned over the unfolding scandal of mismanagement and embezzlement of public funds by the Banks officials. The IRBA found that a former KPMG partner named Dumisani Tshuma, who resigned in 2018 due to allegations of misconduct involving loans from VBS Mutual Bank, was guilty of failure to disclose his conflict of interest in Mutual Bank.

Tshuma and another KPMG partner, Sipho Malaba who was a member of the VBS audit team and also the engagement partner rewarded with alleged bribes worth R34m in loan facilities by VBS, were both subjected to a disciplinary inquiry for their shared role and nondisclosure of the loans facility given to a company called Betanologix. During the inquiry it was revealed that in March 2016, the two, on behalf of Betanologix applied for and were granted a loan facility by VBS. The loan facility had no repayments arrangements since the account was opened, resulting in an outstanding debt of R9.6m days before the bank went down. Both their wives were directors at Betanologix.

[107] South Africa. 2005. Auditing Profession Act No. 26 of 2005:
[108] Khumalo, K. 2017. Board for Auditors Claims Evasion by KPMG. *IOL*: 1–7. https://www.iol.co.za/business-report/board-for-auditors-claims-evasion-by-kpmg-11476809 30 April 2018.
[109] Lynley Donnelly, "KPMG woes deepen after VBS bank scandal" (Johannesburg, 15 Apr 2018)

When they were asked to provide clarity about the company and they denied the existence of such loan facilities with VBS. They also denied any links to Betanologix. Tshuma also denied withdrawing R200 000 from Betanologix accounts for himself, saying it was on behalf of his wife who did not have her own bank account after he had denied any knowledge of Betanologix. Tshuma was given a penalty fine of R200.000 by IRBA. The investigation revealed that Sipho Malaba was aware that the bank was in the red by about R1 billion, regardless of these facts he continued and signed off VBS's financials and took a R34 million bribe.

During the investigation, the Reserve Bank estimated that as much as 75% of the mutual bank's assets had been stolen by its executives and directors.[110] The disgraced KPMG agreed to pay R500 million to settle a three-year lawsuit by VBS Mutual Bank liquidator. In July 2024, the former VBS chairperson was sentenced to an effective 15 years imprisonment as part of a plea bargaining deal. It was further recommended that KPMG be held liable for damages incurred by the VBS curator, National Treasury and the Prudential Authority.

In another saga, KPMG as auditors for a Gupta' company, Oakbay Investments, was alleged to have looked away when it received half a billion rand of illicit funds from a foreign country. The transactions which had enough evidence for KPMG to can deduce that something was wrong, was described in Oakbay's audited financials, yet KPMG did not qualify its audit opinions. It bore multiple hallmarks of Oakbay Investments being utilised as cover to bring illicit money into South Africa. It was clear that suspicious foreign entities paid millions into some dormant local shell company for non-existing shares and the proceeds were moved to Oakbay Investments.

In one of the deals, Fidelity Enterprises Limited, a company registered in Dubai, had agreed to pay R350-million for 49% shares of Micawber 495, a dormant Gupta company used as a coal mining vehicle. Subsequently Fidelity ended up paying Oakbay R256-million more in advances in the final year that KPMG audited Oakbay, yet Micawber 495 shares were never transferred to Fidelity.[111]

The leaked information about the Gupta family further reveal in another debacle that Ashish Gupta, a 26 year old Gupta member based in the USA bought 35% of Keriscan from Oakbay for $17.5-million in another deal linked to a Gupta coal license. It transpired that Oakbay bought Keriscan off the shelf for R100 two weeks before the deal. According to Oakbay's 2014 KPMG audited financials; Ashish paid $10-million to Oakbay for that transaction.[112]

In total, KPMG audited 30 Gupta companies in South Africa, and there is no tangible evidence that they knowingly participated in corrupt money laundering schemes, kickbacks and any fraudulent activities.[113] They also denied that they facilitated any corruption, yet all these matters were glaring in their face and they failed to report the suspicions as is required by law. Too many, questions remains unanswered by the Audit Firm. Questions like: How could the firm not pick up such straight forward money laundering schemes, what exactly were they auditing if they could not pickup such anomalies. And why KPMG CEO (Moses Kgosana) accepted and attended an invite to the Gupta wedding? Were they paid astronomical fees to look the other way?

[110] Lynley Donnelly *op sit*
[111] Amabhungane and Scorpio, "The #GuptaLeaks: KPMG missed more money laundering red flags" *Daily Maverick* (Johannesburg, 27 November 2017)
https://www.dailymaverick.co.za/article/2017-11-27-amabhungane-scorpioguptaleaks-kpmg-missed-more-money-laundering-red-flags/
[112] Amabhungane and Scorpio *op sit.*
[113] Shoaib, A. 2018. KPMG South Africa to Review Past Audit Work Amid Fresh Scandal. Accountancy Age: 1–3. https://www.accountancyage.com/2018/04/16/kpmgsouth-africa-review-past-audit-work-amid-fresh-scandal/ 28 April 2018.

As more about the family's financial clout surfaced, KPMG SA in April 2016 announced that it was cutting all ties with Gupta entities. Due to all these professional mishaps, the firm lost the chunk of its clientele. Big industries like Foschini, Sygnia Asset Management, and Telkom stopped using their services. KPMG SA chairperson resigned. The Firm transformed its management structure and its governance and audit quality procedures in an attempt to restore its reputation and credibility.

As investigations and enquiries continue, the ultimate sanction that KPMG could face could either be the suspension of the operating license if prima facie evidence is uncovered. The biggest worry is that KPMG also audits the books of major South African banks, namely Nedbank, Absa, Investec and Standard Bank. It collapse might have serious implications for the South African Banking industry.

4.3.2 McKinsey

A South African Treasury investigation report[114] on state capture revealed how the Gupta friends highly placed in Transnet and Eskom helped them to loot Transnet and Eskom. The report contained information about dodgy deals concluded by former Eskom and Transnet senior officials and implicated multinational advisory firm, McKinsey. It also referred to the contract signed with Tegeta Exploration and Resources, a company owned by Guptas and Duduzane Zuma, former president Zuma's son, for a 10-year multibillion-rand coal supply. Tegeta was paid at inflated prices even though it supplied less and inferior quality coal than contracted. It also found that China South Rail (CSR), a company that is alleged to have given kickbacks of more than R5 billion to Gupta-linked companies, was unjustifiably offered a tender worth multibillion Rands by Transnet even though it did not meet the tender specifications. McKinsey was the advisory firm during these transactions and never questioned the legitimacy of such transactions.

In the report, it is alleged that McKinsey paid for Anoj Singh, then CFO at both Transnet and Eskom, to go on holiday to Dubai, UK, Russia and Germany, after he renewed their contract with Transnet from a cost base of R25 million to R49 million. A day after this extension was approved he was invited to a conference of CFOs to be held in London by McKinsey. McKinsey also facilitated Singh's eight-day trip to Dubai, further securing his visas and accommodation at the Langham, a five-star hotel in London, as well as the Sheraton Frankfurt Airport Hotel in transit.[115]

Few weeks after he returned from the McKinsey sponsored London trip, Singh recommended McKinsey to Transnet as an advisory services provider for the procurement of the 1 064 locomotives, which was initially costed at R38.6 billion but increased to R54 billion. McKinsey was overall the highest-ranking bidder in that process. The Guptas and their friends made R5 billion in kickbacks on that deal.

During that same period it was also found that, as Singh was appointed to his other role as Eskom CFO, he received six deposits totaling R16 million suspected to be kickbacks in his personal account in one month. It was not clear how the balance of R19 million in his account was accumulated, a matter that was investigated by Directorate for Priority Crime Investigation (DPCI). Singh did attend the CFO conference the following year via Moscow and Dubai at McKinsey cost again regardless of the mounting revelations.

[114] Nicki Gules And Sipho Masondo, "Treasury drops looting bomb" *News24* (Johannesburg, 29 July 2018) https://www.news24.com/SouthAfrica/News/treasury-drops-looting-bomb-20180729-4
[115] Nicki Gules And Sipho Masondo, "Treasury drops looting bomb" News24 (Johannesburg, 29 July 2018)

The Treasury report also found that Singh further assisted Regiments Capital to become McKinsey's partner after Nedbank Capital was terminated over a conflict of interest. This made McKinsey's contract value, through unjustified scope extensions, to increase from R35.2 million to R267 million. When Eric Wood, the founder Regiments Capital left, the contract was ceded to his new company called Trillian. In total, Transnet paid about R3.1 billion to McKinsey, Trillian and Regiments partnership contracts.[116]

McKinsey's relations with Trillian were extended to Eskom operations as Singh became Eskom's CFO. This deal collapsed as corruption allegations that damaged McKinsey's reputation surfaced. The allegations that Trillian was laundering money and was controlled by the Gupta family who were friends of Jacob Zuma started to surface. McKinsey denied that it knowingly allowed funds to be diverted from Eskom to a Trillian as a way to secure the contract even though there was evidence in letter that McKinsey wrote to Eskom, instructing them to make Trillian, a Gupta-linked firm, an unlawful R600-million payment. The transaction was unlawful in that there was no legal obligation for Eskom to make such payments to Trillian, considering the fact that there was no valid contract between Eskom, McKinsey and Trillian at the time. The payments, based on McKinsey instructions, were made out of fraudulently generated invoices, enough reason to be suspected as money laundering activities. [117]

Because of these allegations of irregularities in Eskom's agreement with Trillian, Eskom's Assurance and Forensics was requested to investigate. Their interim report assisted by G9 Forensics found that McKinsey made R1.6 billion in service fees and had projected an extra R7.8 billion in future earnings on the same deal. When the corruption around the deal was exposed, McKinsey released a statement expressing its embarrassment in errors it made at Eskom. But at the same time denying any wrong doing declaring to pay back the service fee it collected.[118]

The Eskom deal allegedly violated a number of laws and most importantly, audit regulations and codes of conduct. McKinsey has since admitted their involvement in the controversy, despite the absence of intention, it is clear that professional standards were violated and they continued to deny charges of corruption and bribery. The firm has since been publicly condemned by civil society organizations, and in the process it lost its major South African clientele, especially Banks who had declared to cut ties with the firm and refused future renewals.

4.3.3 Ernst & Young

Transnet has also been accused of procurement irregularities and attempted cover-up on capital projects overspending. In February 2009 the parastatal extended its internal auditing contract period with Ernst & Young to 2013 when the actual due date for renewal was 2010, at the cost of R400 million annually to without following procedures.

For the public, the investors and the audit profession, failure by an auditor to identify fraudulent irregularities can have awful consequences for all, but then it can be an opportunity for another firm to make cash if selected to clean up afterwards. In a typical case, Transnet's instituted an investigation with the use of their external auditors, Deloitte & Touche, who after investigations found "reportable irregularities", in terms of the Auditing Profession Act, in a contract concluded by the then Transnet Freight Rail (TFR) CEO Siyabonga Gama. Gama was found to have allegedly breached procurement procedures in relation to the locomotive contract that

[116] Nicki Gules *op sit*

[117] Ted Blom, *"Unplugging corruption at Eskom"* (A report by the Organisation Undoing Tax Abuse (OUTA) to the Portfolio Committee on Public Enterprises. 18 October 2017)

[118] Ms D Rantho, "Eskom Inquiry: G9 Consulting Services" (Chairman's opening statement at the Portfolio Committee on Public Enterprise meeting 28 February 2018)

he signed which was initially costed at R867-million, but subsequently escalated by over R5.4-billion. Deloitte & Touché reported the alleged irregularity in terms of Section 45(1) of the APA to the IRBA.

Ernst & Young was subsequently accused of overlooking serious governance-flouting observations at Transnet Rail Engineering and Transnet Capital Projects.[119] There were claims made that the Firm's lead partner, who discovered and reported the irregularities was swopped with another partner tasked to cleanup and change these findings. In terms of the allegations, the initial lead partner found that Transnet:

- Had approved R8.7bn spending for the Ngqura container terminal project, but this amount escalated by 23% to R10.7bn.
- The company also budgeted R3bn for widening the Durban harbor entrance, but the project cost escalated by R800m more.
- The Cape Town container terminal expansion budget of R4.2bn was approved, compared to the final cost of R4.9bn.
- Transnet Pipelines was budgeted at R11.6bn, which increased by R700m.
- The Orex feasibility study (Phase 2) was budget at R142m, escalating by 34% contrary to the Board of Directors' resolution.[120]

These revelations resulted in allegations of irregular, fruitless and wasteful expenditures in the amount of R18-million as contemplated by the Public Finance Management Act of 1999. It still baffles many as to what role Ernst & Young played in the whole debacle, and how could they not report these reportable matters instead turned a blind eye and changed their lead auditor at Transnet.

Ernst & Young was also involved in a R100-million lawsuit against Eskom in which a former chief information officer who was fired by the company, was suing Eskom for incurring loss for future earnings, pain and suffering and legal fees. The employee claims that Eskom relied on a report by Ernst & Young during his disciplinary hearing which led to him being dismissed from work, but that a full version of the same report, which was concealed during the hearing, exonerated him. He accused Eskom and Ernst & Young of colluding to hide the full report with the intention to get him fired.

The Standing Committee on Public Accounts (South Africa) (Scopa) is also interested in the services that PwC and Ernst & Young offered to South African Airways. Both would appear to have captured SAA during the tenure of Dudu Myeni (a Gupta Family supporter) as the then chairperson of SAA. Scopa wants to see details of all the work done by both for the airline after a damning report on the airline's 2017 accounts by the auditor-general. The auditor-general qualified his audit opinion on SAA for a variety of reasons including the failure to maintain complete record of irregular expenditure, and the fruitless and wasteful expenditure that was discovered.

The report also raised issues with SAA's record of property, aircraft, equipment and inventory. The report raised questions about how PwC was able to give SAA clean audit opinions for

[119] IOL, "Transnet accused of R5.4bn cover-up "*Business Report* (Johannesburg, 26 November 2009)
[120] *Supra.*

each year between 2012 and 2016 and what role Ernst & Young played in the whole debacle. These matters continue to be investigated.

4.3.4 Deloitte & Touche

Deloitte Africa has been implicated in some of the biggest South African corporate failures ever seen including African Bank, Steinhoff and LeisureNet to mention a few.

4.3.4.1.1 African Bank

Deloitte Africa has been implicated in some of the corporate failures reported on. Their involvement has been mentioned in the most damaging demise of African Bank Limited and its holding company, the African Bank Investments Limited. The Bank was found to have flouted accounting standard IAS 39 requirements that deals with the recognition and measurement of financial instruments when it comes to the impairment of loans, and the Bank was thereafter placed under curatorship.[121] The Myburgh Commission found Deloitte to be implicated in producing the Bank's fraudulent auditing reports and fined them R2 million. It was argued that Deloitte as the bank's auditing firm knowingly, should not have allowed this. The Bank was declared an unsecured lender and placed under curatorship by the SA Reserve Bank, and its shareholders forfeited billions of Rands.[122]

IRBA launched an investigating committee that investigated the complaint of potential improper conduct by the auditor in terms of Section 48 of the Auditing Professions Act. And subsequently in terms of Section 49, the auditors were charged with improper conduct based on sufficient existing grounds. Formal charge sheets were issued and a formal disciplinary hearing was undertaken in terms of Section 50.

The hearing had to establish whether Deloitte auditors applied "professional skepticism" in their deliberations, and whether they did enough to ensure that African Bank provided adequately for bad debt. The disciplinary hearing took two-year, from 2018 to 2020. Mgcinisihlalo Jordan, Deloitte's main partner and Deputy CEO, was slapped with 10 charges of improper conduct, malpractice charges and dishonesty. His colleague, Danie Crowther, was slapped with one charge of improper conduct. Jordan was found guilty of 5 charges, fined R800 000 and suspended from practice for two years, upheld on condition that he does not sign audit reports and does acting as engagement partner for 3 years. Crowther was exonerated of the improper conduct charge.

4.3.4.2 Steinhoff

The shocking financial collapse of Steinhoff International Holdings, one of the top 10 companies on the Johannesburg Stock Exchange, left the South African corporate world in disgust. Steinhoff International, was a global retail company with its largest operations based in South African. Steinhoff was incorporated in Netherlands, but its head office was in South Africa. The collapse came about after the company's external auditors refused to sign off its 2017 financial statements, and subsequently the company's Chief Executive, Markus Jooste resigned.

[121] Justin Brown, "Deloitte partners charged" Fin 24 (Johannesburg 25 March 2018) https://www.fin24.com/Companies/Retail/deloitte-partners-charged-20180323
[122] Justin Brown, *op sit*

Its management was accused of misstatements of its financials by hiding loses and inflating earnings. Deloitte was investigated for overlooking these irregularities in Steinhoff's accounting processes. Steinhoff lost more than R100-billion, within 48 hours, almost the same amount the Guptas are accused of looting South Africa over a decade.

In return, the South African police asked Interpol to help investigate Steinhoff International Holdings NV. This request led to Steinhoff and their auditing firm being investigated by regulators in Germany, Netherlands and other countries where they operate. Interpol could also help connect the dots about the owners of Conforama in France and Mattress Firm in the US which are some of the implicated companies.

Steinhoff was a real classic case of corporate governance failure. On the Steinhoff saga, Naudé in his management report, argued that the company's board attempted to provide ethical and effective leadership over the years, but the attempts were inadequate (Naudé et al, 2018:p17).[123] The collapse was also an indication that a two-tier board structure has serious limitations, and that an all-powerful Chief Executive was a danger to existence of that company. In addition, serious reservations were made about the earlier years external auditors who signed off on financial statements of the company. And Deloitte was confirmed as the firm that did the auditing work for Steinhoff for most years.

Deloitte was investigated and disciplinary action being taken by the IRBA for the auditing work that they did on Steinhoff's financial statements for the years 2014, 2015 and 2016. The investigation established that there was complicity in wrongdoing between the auditors, Steinhoff's directors, and fund managers by creating an enabling environment conducive to money laundering.

The CEO of Steinhoff International, Marcus Jooste upended two major fraud cases against him in South Africa and Germany. He and Dirk Schreiber, Steinhoff's former European finance chief, were accused of misstatements in the companies' annual financial statements and annual reports for the period from 2014 to 2016 and for the 2017 half-year. It was revealed that they made or published false, misleading, or deceptive statements about Steinhoff Enterprises financials.[124]

These material misstatements were uncovered by the company's board and subsequently the Board appointed PwC to investigate the company's financial statements and annual reports.[125] The investigation established that the CEO had too much influence over the auditors thus ensuring that the auditors overlooked certain matters that resulted in material misstatement of the company financials statements. The South African Authorities decided not to prosecute Schreiber because he co-operated with its investigation and provided evidence, but Marcus Jooste the CEO was prosecuted.[126]

[123] Naudé, P., Hamilton, B. & Ungerer, M. 2018. *Business Perspectives on the Steinhoff Saga*. Cape Town. https://www.usb.ac.za/wp-content/uploads/2018/06/USB-Management-Report-Steinhoff-Saga.pdf.

[124] Ensor, L. 2018. Steinhoff Director Spills the Beans About Accounting Irregularities and Jooste's Disappearing Act. Business Day: 1–2. https://www.businesslive.co.za/bd/companies/retail-and-consumer/2018-01-31, 12 December 2018.

[125] Ann Crotty,"Deloitte in spotlight again with African Bank hearing" *Bussiness Day* (Johannesburg 19 March 2018) https://www.businesslive.co.za/bd/companies/financial-services/2018-03-19-deloitte-in-spotlight-again-with-african-bank-hearing/

[126] Kew, J. & Bowker, J. 2018. We're Not Friends - Steinhoff Ex-CFO Blames Jooste, Auditors for Accounting Scandal. *Fin24*: 1–4. https://www.fin24.com/Companies/Retail/were-not-friends-steinhoff-ex-cfo-blames-jooste-auditors-for-accounting-scandal-20180829 12 December 2018.

Marcus Jooste faced charges of fraud, racketeering, and contravention of the Financial Markets Act 19 0f 2012 (FMA) at the Specialized Commercial Crimes Court. The hearing held was open to the public due to increased public pressure. The expectation of the public was for action to be taken against powerful parties regarded as complicit in any money laundering irregularities in the country. Jooste was found guilty for misstatement of financial statements and fined R475 millions, and he committed suicide 2 days after the verdict.

The penalty order indicated that he made misstatements by fabricating operating profits, cash and cash equivalents, goodwill balances, and other financial figures, either by creating transactions with no economic substance or by omitting crucial information required by Reporting Standards. He literary overstated the company operating profits, cash balances, and other financial metrics, misrepresenting Steinhoff financial status to investors, lenders, and creditors.

The court case in Germany sentenced Dirk Schreiber, Steinhoff's former European finance chief, to three-and-a-half years' imprisonment for accounting violations and aiding fraud. He was the first person to be jailed for the Steinhoff fraud. Jooste was also charged in the German case but failed to appear in court. Schreiber was granted leniency because he co-operated extensively with the investigation.

The court in Germany also convicted ex-director Siegmar Schmidt and he got a two years suspended sentence. Both Schreiber and Schmidt had their sentences reduced by a year because the investigation took too long the court said, making Schreiber's effective sentence two-and-a-half years.[127]

4.3.4.3 LeisureNet

Deloitte had also been found to have been the auditor of LeisureNet when the group failed it was placed under a liquidation order. At the time LeisureNet ran a business of 85 Health & Racquet Club gym facilities in the country with over 900 000 members. At an IRBA enquiry it was discovered that the group's collapse was due to 3 factors, first was the change in its accounting policy, second was the role played by the auditors in financial misstatements of reports, and thirdly, the reckless way directors carried-on the business of LeisureNet with the intentions to defraud its creditors.

It was established that a senior partner at Deloitte, then LeisureNet auditing firm, helped the company directors to falsify a note in the company's annual financial statements which was intended to mislead the SA Reserve Bank with full knowledge of some of LeisureNet board members. The alleged senior partner attended LeisureNet's board meetings as a representative of Deloitte & Touche.

It was found that after the misrepresentation, the senior partner left Deloitte to join Healthland International in Britain. Healthland International, a foreign entity with 17 subsidiary groups owned 22 operating health clubs and had 17 developing clubs.[128] By then LeisureNet was listed as Healthland International's main shareholder with 57.8% interest and the ex-Deloitte

[127] Moonstone Information, "Jooste's death won't affect Steinhoff investigation", Posted on 25 March 2024 Refineryhttps://www.moonstone.co.za/joostes-death-wont-affect-fscas-steinhoff-investigation/

[128] Leatitia Watson, "Policy a problem at LeisureNet" *Fin24* (Johannesburg,19 June 2001) https://www.fin24.com/Companies/Policy-a-problem-at-LeisureNet-20010619

partner had a 1.8% interest. LeisureNet also sponsored Healthland International's substantial debt commitments to the value of more than €82m (R921m then) which placed substantive pressure on LeisureNet.

The story is that, Healthland International concluded management agreements with Ajax Way Investments, Pinnacle and Clockwork, companies that were associated to LeisureNet directors. These companies were omitted in the annual financial statements with the intention not to disclose them to the SA Reserve Bank as per Deloitte's advice. Instead they were replaced in the note with different BVI companies named Kinsman, Moreland and Baycroft also linked and associated LeisureNet directors. The whole modus operandi was to launder money out of the country to Healthland International, intentionally creating an environment that would make LeisureNet to crush.

In the process a Black Empowerment investment company, Sekunjalo, launched an unprecedented R200m law suit for damages against Deloitte & Touche over the losses it claims to have suffered when Leisurenet collapsed. The matter is still pending.

4.3.5 SAP

SAP, a German software maker, and McKinsey suspended and terminated some of its employees after launching internal investigations to probe their dealings with Gupta-linked companies and payments of kickbacks for the help they got to win tender contracts, to a firm in which Zuma's son, Duduzane, had an indirect stake. It is alleged that SAP contracted with 3-D printing, a company co-owned by Duduzane and the Guptas, and promised a 10% commission if 3-D could facilitate a deal with Transnet to sign a software contract with SAP for at least $7.3 million.[129]

Evidence revealed that SAP paid the 3-D printing company kickbacks almost as much as the contract's total value. SAP posted a denial statement on its website for paying any kickbacks to 3-D, but the statement has been subsequently removed from website, with SAP claiming the matter was pending investigation and under judicial consideration and therefore prohibited from public discussion elsewhere.

Another SAP mishap was also choosing Global Softech Solutions as a supplier development partner on an R800-million Transnet contract. Global Softech Solutions was another Gupta owned IT Company. At the time Global Softech Solutions had a turnover of R53 million. It would have made R500-million if the deal did not fail due to Government intervening and stopping the process.

4.3.6 PwC

As discussed previously, in 2017 Eskom signed a contract with KPMG to introduce a new supply chain management operating model at a cost of R69.8-million, 40% of which was meant to go to Nkonki, a very small local player in the industry, as their local partner.[130] During the same period they signed a new R3.6 billion over two years' worth, "at risk" consulting contract

[129] AmaBhungane and Scorpio, "#GuptaLeaks: Software giant paid Gupta front R100m 'kickbacks' for state business" *News24* (Johannesburg, 11 July 2017)

[130] amaBhungan, Eskom's new billion-rand consulting deal for Essa & Co (The daily Maveric: The Nkonki Pact Part 2.29 March 2018) https://www.dailymaverick.co.za/article/2018-03-29-amabhungane-the-nkonki-pact-part-2-eskoms-new-billion-rand-consulting-deal-for-essa-co/

for a capital scrubbing project with PwC, a professional services company with revenue of $37.7-billion.

PwC decided to choose Nkonki as its supplier development partner too, which was an Eskom requirement to help empower local players in the industry thus create jobs. The two firms had already worked together at Transnet and SAA. Nkonki had just been bought by Salim Essa (using Mitesh Patel as a front), a Gupta lieutenant, through an 88% management buy-out financed from the Gupta Family coffers. Nkonki did not bid to participate for this tender as a local company but PwC was somehow allowed through this nexus between the two Audit Firms by Eskom directors just like McKinsey was forced to partner with Trillian, another unknown Gupta owned company in another Eskom cancelled controversial contract.

In return PwC's hourly fees were increased from quoted R550 to R2, 836, and their scope was expanded so as to give Nkonki a big cut. All of this coincided with the Gupta-funded takeover of Nkonki. The Guptas were to get 65% of Nkonki's profits. Nkonki were initially going to make R1.1-billion out of the contract, figures that Eskom disputed but refused to supply the actuals claiming client info confidentiality. When the scandals broke, and the public outcry and backlash to Eskom increased, the contract with PwC was reviewed and the costs reduced. PwC ultimately received around R95 million, whilst Nkonki received R17.7-million in return, which was less than 30% of what was initially agreed to. PwC subsequently denied to have knowingly partnered with Nkonki, a Gupta-linked firm, or that the lucrative tender contract it signed with Eskom was depending on paying facilitation fees to a politically-connected partner.

The Guptas claimed pure coincidence in that Nkonki was appointed to both contracts within weeks whilst the auditing firms claim to have not known that Nkonki was connected to the Gupta family when they signed the contracts. Directors and executives that were involved in these transactions were purged out of Eskom. The exact nature of the work that PwC did for Eskom remains unclear. Nkonki confirmed to have received R16.1-million from this partnership over and above the initial R17.7 million paid earlier, and another R14-million from the KPMG contract signed in January 2017.

4.4 GOVERNMENT AND BUSINESS REACTION:

The South African government and business has been overwhelmed by these unethical scandals and government used its justice system full force, whilst businesses like banks withdrew their services to implicated companies. The private sector business also withdrew the services of implicated auditing firms. McKinsey and KPMG were the hardest hit. SizweNtsalubaGobodo , an auditing firm that was subsequently appointed by Transnet and Eskom's to audit them, was the one that disclosed the irregularities at the two companies to the Regulator.

In one affidavit filed in the North Gauteng High Court, the National Prosecuting Authority of South Africa accused McKinsey for colluding with Trillian and Eskom in stealing R1.6bn from Eskom. McKinsey was accused of falsifying and fraudulently invoicing Eskom for no services rendered with the help of Eskom officials. Evidence revealed that payments to Trillian and McKinsey which were made by Eskom's amounted to the proceeds of crime, "namely fraud, theft, corruption and money laundering".[131] It was for the first time that legal action was taken against those implicated in Public Protector's investigation, supported by various media disclosures. As a follow-up, Government launched various investigations inclusive of the "State Capture Inquiry." Due to lack of substantive evidence, all these investigations could not implicate McKinsey for any wrong conduct. The firm has kept on denying wrongdoing but offered to pay back to Eskom the money paid for services rendered.

[131] https://www.timeslive.co.za/news/south-africa/2018-01-17-npa-throws-the-book-at-mckinsey-for-theft-of-r16bn-from-eskom/

In terms of Joint Rule 159, the Minister of Finance tabled in Parliament the General Laws Amendment Bill [B18-2022],[132] The Parliamentary ATC No125-2022 confirmed the submission of the Bill to the Standing Committee on Finance (SCOF) and the Select Committee on Finance (SECOF).[133] Cabinet approved the Bill, demonstrating Cabinet's commitment to fight corruption, laundering and terrorism financing. After the publication an Interdepartmental and Agency Committee on AML was established. It was chaired by the Director-General of National Treasury, and its aim was to coordinate any legal gaps established between various Government departments and Agencies and make recommendations that seek to strengthen the country's anti- money-Laundering laws. Recommendations were made to amend five pieces of legislation relating to fighting financial crimes.

The proposed amendments administered by different Ministers, were intended to close any identified gaps relating to the adequacy of laws and legal frameworks that were identified in the Mutual Evaluation Report (MER) as relating to the 40 FATF Recommendations. This was a significant step by the Government towards addressing all the identified in the MER report and the enactment of the Bill into law was seen as an attempt to improve the country's adherence to international best practices intended to combating corruption.

As far as private business is concerned, KPMG's relationship with the Guptas and the more recently collapsed VBS mutual bank prompted a lot of private companies to terminate their relationship with the auditing firm. JSE-listed Asset Manager Sygnia, with a market value of R1.4-billion, was the first to fire KPMG over its alleged role in state capture debacle. They were followed by clients such as retail companies, mining companies, production companies, Banks and many others as was previously indicated.

As a last straw, South African banks, also withdrew their services to all Gupta owned companies amid allegations of state capture and allegations of money laundering. This actually caused turmoil to the Gupta company operations; they could not function, could not pay employee salaries, and could not pay their debtors.

In a last ditch to stay afloat, all the 20 Gupta-owned companies, brought an urgent application at the North Gauteng High Court (*Annex Distribution (Pty) Ltd and Others v Bank of Baroda*)[134] in a last effort to retain banking services including the Bank of Baroda, an Indian bank that was withdrawing from South Africa amid the scandals. The Gauteng High Court (Pretoria) Judge Hans Fabricius dismissed the Guptas' court bid to prevent the bank from closing its accounts. They were forced to withdraw their monies out of the banks, sell their companies very fast whilst facing legal challenges on the other side. They escaped to India and subsequently to Dubai, UAE.

4.5 CONCLUSION:

Good corporate governance practices were highlighted as the biggest shortcoming of the scandals and failures discussed above. The scandals provided an opportunity to examine and analyse encountered challenges and ethical issues in auditing big companies. Businesses have for many years relied on the Audit Firms reputation for their statutory audits, and similarly investors also relied on the same auditor's reputation before making a decision to invest in any business.

This Auditor reputation plays an additional important role in mitigating information asymmetry problems because many clients are repeat users of their services and the information. The

[132] General Laws (Anti-Money Laundering and Combating Terrorism Financing) Amendment Bill [B18-2022] https://www.parliament.gov.za/bill/2304475

[133] https://www.parliament.gov.za/storage/app/media/Docs/atc/04220701-ef65-4348-8032-4a41b6dc6f8c.pdf

[134] *Annex Distribution (Pty) Ltd and Others v Bank of Baroda* (52590/2017) [2017] ZAGPPHC 608; 2018 (1) SA 562 (GP) (21 September 2017)

scandals, however, have put a negative dent on the audit reputation effect. Krishnamurthy et al (2006),[135] used a sample of former Arthur Andersen clients, to illustrate that reputation effects become negative when the market perceive auditor's independence to be threatened in addition to audit quality.[136]

These scandals have plagued the auditing profession over a long period of time leading to an atmosphere of distrust and reputational doubts that has led to professional doubts. But more-so the closure of a large "black" auditing firm, Nkonki, which impacted on the very essence of the Auditor transformation process in South Africa. It also lead to the removal of auditor's from the auditor's roll and to substantial fines for the auditing profession. However, to attribute most of the problems to the auditing profession would be to believe that the auditing profession is rife with crooks, a conclusion that is untrue.

Government prompt reaction to demonstrate commitment has been seen to tackle the problems head-on. Government, in reaction tabled the General Laws Amendment Bill in line with FATF and MER prescriptions. On one side, large businesses terminated their relations with some of the audit firms involved, with the Banks following suit by closing accounts linked to the scandals. Thousands of employees lost their jobs because of these scandals and in return the JSA made massive loses.

It is evident that the entry of Gupta Family created more problems for the profession, as they brandished their power, they incited a backlash, not only from ordinary South Africans only, but also from political constituencies that got concerned that the brothers were putting the country's economic health at risk using their proximity to the high office in the land. Thus Government Agencies like the Public Protector's Office got irked and started to investigate the level of capture that the brothers had on government.

As the stories around their shenanigans developed, the Gupta brothers fled to Dubai. Charges were pressed by IRBA against KPMG SA, Deloitte & Touché and others for audit work that they did circumventing the full legal oversight. With the subsequent investigations, top partners at McKinseys, KPMG, HSBC, Standard Chartered and SAP were terminated for their connection to the Gupta businesses.

Bell Pottinger's (the P.R. firm) credibility took a knock after trying to stir up racial resentments at the Guptas' behest. What is striking is how many of these multinationals firms have blindly done business with the Guptas, making a lot of money, only to wake up sinking in scandals and then claim amnesia.

There are numerous other scandalous examples that have implicated the big auditing firms in suspect corporate activities, but every time, they come out clean claiming innocence because the regulating authorities do not have experienced staff to can pin faults on them and verify them, with the exception of developed countries. The problem most of the time is a skills problem and thus audit firms escape scot-free from accountability.

[135] S. Krishnamurthy, J. Zhou, N. Zhou, Auditor reputation, auditor independence, and the stock-market impact of Andersen's indictment on its client firms, Contemporary Accounting Research, 23 (2) (2006), pp. 465-490
[136] Krishnamurthy et al (2006) op sit.

This chapter was all about that insight into the businesses belonging to the Gupta family and how they maneuvered their interests in the President's Office, into the big audit firms and the state owned companies. And how Government and Business reacted.

Chapter 5: A comparable study with the UK and the USA

5.1 INTRODUCTION:

Considering the fact that money laundering legislation is a global phenomenon and crosses borders that is basis for the formation of Financial Action Task Force (FATF) to prescribe international standards that global governments could operate within. South Africa joined developed countries like UK and the US as a FATF member state obliged to adhere to the FATF global standards meant to combat financial crimes like money laundering and related activities.

Since 1990, the United Kingdom has also been a member state that subscribes to FATF standards too. The country has undertaken a number of regulatory changes to strengthen its legal framework meant to tackle money laundering and terrorist financing since its initial assessment in 2018. The UK is a major global economic hub, therefore it is important for it to ensure that its regulatory framework is aligned with international standards.

FATF's International standards and guidelines have influenced UK's KYC regulations. For UK to secure its global reputation and maintain its reliable financial status, compliance with FATF standards has not just been a legal prerequisite but an imperative strategy. Its efforts to Implement and sustain its KYC process required substantial investments in technology, recruitment of the right people, and training. It also came with huge financial and operational cost implications.[137] Other efforts being engaged are the ongoing global debates about different ways that can be employed to strengthen auditor independence, and considerations related to governance and transparency of audit firms, most notably in the USA, UK and European countries.

In the US, KYC regulations are prescribed in the Bank Secrecy Act (BSA) and the Patriot Act. The two Acts require financial institutions to establish Customer Identification Programs (CIPs), conduct client due diligence, and monitor client transactions for any suspect anomalies. The last FATF mutual assessment report on US, dated March 2024[138], resolved that the United States was 9 compliant of the 40 Recommendations, 23 largely compliant, 5 partially compliant on 5 and 3 non-compliant compared to the 40 FATF Recommendations, resulting in being upgraded to 24 on technically compliance.[139]

In Africa, most countries have been removed as FATF member states due to failure to comply. South Africa has remained and was put on the greylist and struggles to get off it since still having a few outstanding noncompliance issues to address. March 2024 countries like Uganda, Gibraltar, Barbados, and the UAE getting removed from the monitoring list in acknowledgement of their significant progress in rectifying the strategic AML deficiencies. Botswana, Mauritius, Morocco, and Zimbabwe were also removed from the greylist. South Africa still had five outstanding technical deficiencies out of the 22 raised by FATF to address. This status had become a reputational blow and economic setback for South Africa and continued to deter potential foreign investments. South Africa's was also criticised by FATF for lack of commitment to prosecuting state capture criminal linked individuals as reported by the Zondo Commission.

The final State Capture report released in June 2022, revealed how the private sector enabled the actual state capture, leading to public pressure insisting that the state should recover

[137] Financial Action Task Force (FATF), 'Anti-Money Laundering and Counter-Terrorist Financing Measures: United Kingdom: Mutual Evaluation Report', December 2018, p. 110, para. 288.
[138] FATF (2024), Anti-money laundering and counter-terrorist financing measures – United States, 7th Enhanced Follow-up Report, FATF, Paris https://www.fatf-gafi.org/content/fatf-gafi/en/publications/Mutualevaluations/united-states-fur2024.html
[139] *Op sit*

losses it suffered against anyone involved in corrupt conduct or anyone who benefitted directly or indirectly in looting the state entities. Auditors were already being accused of failure to detect irregular state capture transactions that saw the state being robbed billions of Rands. The said failure to detect exposed auditors to legal liabilities by companies involved, affected third parties as well as by the regulator, IRBA. The regulator was been put under political pressure to investigate auditing firms involved in these alleged criminal activities and establish their role in failure to detect the fraud and corruption that led to these high profile scandals.

In a March 2024 plenary recently held by FATF in Paris, it was alluded that South Africa still needed stronger supervision of professionals like accountants and lawyers, to ensure that these professionals were not involved or colluding with criminal elements. It was further said that the country needed to improve its collaborative efforts with other countries in investigations and confiscations of illicit assets obtained through criminal activities. The country also need to inforce targeted economic sanctions against wrongdoers. During this same plenary, Kenya and Namibia were added for the first time as member states.

The country is due for reassessment by FATF again in February 2025, to see whether it has made any progress. It is unlikely that South Africa would be delisted then, considering the lack of political will to prosecute and convict the many identified culprits that are in various leadership positions. Even though the country has committed to implement action plans to swiftly resolve identified deficiencies required to address money laundering activities.

Based on the analysis gathered so far, in this chapter we intend to draw some lessons learned from the UK and the US in their efforts and attempts to combat money laundering crimes, give a few examples of their respective case studies and make a strong comparable case with regard to the South African status. We thereafter will also include a bit about Terrorism Financing, even though it is not the theme for this research but a future potential area to be investigated.

5.2 THE UK PERSPECTIVE:

Of recently the criminal activities by launderers intended to clean illicit money has been on an increase, through use of companies registered in the UK because they appear to be more legal than those in offshore tax havens, and also because of the strength in value of the sterling pound. The UK's AML legal framework is multifaceted and dynamic and reflects the Government's commitment and political will to ensure the country's financial integrity and alignment with global standards. The Government is forever reviewing its policies and regulations to tackle money laundering than any country in the world, however it has been found to be lacking when it comes to policing its regulations due to lack of resources.

Whilst lack of resources to investigate cases of irregularities and complicity of auditors is a known matter, the UK courts still appears to be too lenient to many Auditing Firms found to be flouting regulations as compared to the US where the Justice Department has made numerous efforts in prosecuting people, sending colluding accountants to prison, and fining a number of Auditing Firms for being involved.

In line with best practice, the government has not only made legislative changes but also engaged structural changes like merging the Assets Recovery Agency (ARA), which is tasked freeze and seize proceeds of crime, with the Serious Organised Crime Agency (SOCA). The Serious Crime Act 2007 as amended by Serious Crime Act 2015 provided for merger. ARA's powers as per Proceeds of Crime Act 2002 were moved to SOCA and Revenue and Customs (RCPO) for coordination purposes.[140]

[140] AML Legislation updates, "Assets Recovery Agency merges into SOCA" *BTC-Latest News* (Lancashire 04 April 2008)

The attempts by laundering criminals have also evolved as the rules of the game changes; they have taken advantage of the UK online system of registering companies by registering a chain of shell companies that are used to wash criminal money before it is legitimized. The recent report from Transparency International's UK arm found that a lot of these companies were used in scandals worth £80 billion in the past decade, and half of the 766 reported companies were said to be based at 8 UK addresses. A tell-tale sign raised suspicions.[141]

As far as other UK legislation is concerned, the of role of detection and reporting of fraud and money laundering has been made a key responsibility of accountants, auditors, and lawyers by the introduction of pieces of laws such the Criminal Justice Act 1993 and the Money-Laundering Regulations 2007.[142] These laws require professionals not to turn a blind eye nor be party to such transactions at whatever price, but instead report them as early as possible to relevant government agencies.

The competition regulator in the UK was recently investigating the Big Four Accounting Firms after the collapse of Carillion. Carillion, with 326 subsidiaries and 199 of them based in the UK, collapsed, and the British Auditing Watchdog opened a probe against KPMG which audited, and colluded with the Firms 169 directors to hiding reportable financial irregularities for the past 19 years.

The UK government has also enhanced its due diligence procedures, as far as "Suspicious Transaction Reporting" (STR) requirements and the "Know your customer" (KYC) rules are concerned to be in line with International standards.[143] A classic example of enforcing these rules by the Financial Services Authority (FSA) is that of Michael Wheelhouse, an anti-money laundering control officer at Sindicatum Holdings Ltd (SHL). He was penalized to the value of £17 500 for breaching FSA's Statement of Principle 7 by not complying with his company's "client compliance checklist" meant to ensure that documentation to verify the client's identity was correct. SHL was also fined £49,000, in part, over its lack of controls around Identification verifications.[144]

Irregularities like these have raised a need for the UK government to further reform its regulations in respect of money laundering than ever before. The target now is to ensure as much as possible that proceeds of corruption are seized without any hesitation, further ensuring a need to require transparencies around any suspect funds ingested in companies from offshore companies. Government agencies are also encouraged to enforce a restraint and disclosure order in respect of local or offshore suspicious real estate acquisitions by UK citizens, contrary to the decision made by the Court of Appeal in the case of *King v Serious Fraud Office*[145] which limited the disclosure to property located in England and Wales only. That decision was upheld on appeal by the House of Lords ([2009] UKHL 17).

The Proceeds of Crime Act 2002 (POCA 2002) as amended by the Serious Organised Crime and Police Act 2005 (SOCPA) and Sanctions and Anti-Money Laundering Act 2018 (SAMLA) are the primary laws that are currently used in the UK to prosecute money laundering cases. SAMLA has been designed to ensure that the country laws keep pace with international standards prescribed by the Financial Action Task Force (FATF). The recommendations outlines the key principles of identifying and verifying customers that should be adopted by financial institutions in various countries. Included in the guidelines are risk assessment

[141] Transparency International UK, " In whose interest: Analysing how corrupt and repressive regimes seek influence and legitimacy through engagement with UK Parliamentarians" (2018)
[142] Austin Mitchell, "The role of accountancy firms in money laundering" (1996).
[143] Fourth Anti-Money Laundering Directive (2015/849/EU)
[144] Financial Services Authority, Final Notice : Michael Wheelhouse http://www.fsa.gov.uk/pubs/final/m-wheelhouse.pdf
[145] *King v Serious Fraud Office* [2008] EWCA Crim 530

procedures, the customer due diligence processes and continuous monitoring systems intended to deter and detect illicit financial activities.

In 2018, FATF initiated an assessment[146] of the UK's compliance efforts with its standards. Subsequently, the country's progress was reassessed and re-rated in 2022. The outcome of the reassessment was that the country was compliant on 24 Recommendations and remained partially compliant on 1 Recommendation (refer the diagram below).[147]

United Kingdom Follow Up Report- 2022: Compliments of the FATF report.

R.1 - Assessing risk & applying risk-based approach	R.2 - National cooperation and coordination	R.3 - Money laundering offence	R.4 - Confiscation and provisional measures	R.5 - Terrorist financing offence	R.6 - Targeted financial sanctions related to terrorism & terrorist financing	R.7 - Targeted financial sanctions related to proliferation	R.8 - Non-profit organisations
LC	C	C	C	C	LC	LC	C

R.9 - Financial institution secrecy laws	R.10 - Customer due diligence	R.11 - Record keeping	R.12 - Politically exposed persons	R.13 - Correspondent banking	R.14 - Money or value transfer services	R.15 - New technologies	R.16 - Wire transfers
C	LC	C	C	C	C	LC	C

R.17 - Reliance on third parties	R.18 - Internal controls and foreign branches and subsidiaries	R.19 - Higher-risk countries	R.20 - Reporting of suspicious transactions	R.21 - Tipping-off and confidentiality	R.22 - DNFBPs: Customer due diligence	R.23 - DNFBPs: Other measures	R.24 - Transparency and beneficial ownership of legal persons
LC	LC	LC	C	C	LC	LC	LC

R.25 - Transparency and beneficial ownership of legal arrangements	R.26 - Regulation and supervision of financial institutions	R.27 - Powers of supervisors	R.28 - Regulation and supervision of DNFBPs	R.29 - Financial intelligence units	R.30 - Responsibilities of law enforcement and investigative authorities	R.31 - Powers of law enforcement and investigative authorities	R.32 - Cash couriers
C	C	C	C	PC	C	C	LC

R.33 - Statistics	R.34 - Guidance and feedback	R.35- Sanctions	R.36 - International instruments	R.37 - Mutual legal assistance	R.38 - Mutual legal assistance: freezing and confiscation	R.39 - Extradition	R.40 - Other forms of international cooperation
LC	C	C	C	LC	C	C	LC

C=Compliant; LC=Largely Compliant; PC=Partially Compliant; NC=Non-Compliant

Ratings:

Technical Compliance ratings which reflect the extent to which the Country has implemented the technical Requirements of FATF Recommendations.

[146] Financial Action Task Force (FATF), 'Anti-Money Laundering and Counter-Terrorist Financing Measures: United Kingdom: Mutual Evaluation Report', December 2018, p. 110, para. 288.

[147] FATF (2022), Anti-money laundering and counter-terrorist financing measures – United Kingdom 1st Regular Follow-up Report, FATF, Paris http://www.fatf-gafi.org/publications/mutualevaluations/documents/fur-united-kingdom2022.html

This comprehensive assessment was intended to review the effectiveness of measures taken by the country to strengthen its AML framework and compliance level with the FATF recommendations.

The assessment concluded that the UK needed to remain in regular follow up, and must continue to report to the FATF on progress it makes on improving its compliance with the standards and the implementation of its AML regime. Since then, the country has made much progress in regard to its technical compliance with FATF Recommendations and the subsequent adoption of its MER. The country has since been upgraded on R.13.[148]

The auditors have also been made to comply with the "know your clients" (KYC) standard as per the Proceeds of Crime Act 2002.[149] The KYC process involves customers' identity verification and risks assessment of potential illegal intentions by the customer towards the business relationship. The Act further requires that should they suspect that money laundering has taken place or is about to take place, they should submit a Suspicious Activity Report (SAR).[150]

The aim about the KYC processes is to ensure the transparency, accountability, and legitimacy of financial transactions. If properly implemented, it will assist to ensure the legitimacy and legality of transactions, identifying high-risk criminal customers, bolster public's confidence in the financial systems, and contribute to greater economic stability and security worldwide.

The POCA 2002 provides for the confiscation or civil recovery of illegally attained proceeds and it contains UK's principal Money Laundering legislation. The Act as amended, under section 298 deals with processes meant to confiscate proceeds of crimes post-conviction, and the use of such confiscated funds to benefit the community.[151]

Part 2 of POCA empowers Directors from the National Crime Agency (NCA), the Public Prosecutions, and the Serious Fraud Office to apply for restraint orders from dissipation of proceeds of such crimes. It also prescribes for the court to consider offering an order for confiscation of illegally attained proceeds against a defendant after being convicted of an offence.
Parts 3 and 4 is meant to provide for Scotland and Northern Ireland's confiscation and restraint orders respectively.
Part 5 of POCA provides for other means of recovery of proceeds of crime which do not require a conviction such as civil recoveries, cash seizures and taxation powers.
Part 6 of the Act enables the NCA to make tax assessments under section 29 of the Taxes Management Act 1970. Specifically for instances where the source of income is suspected and cannot be accounted for. This Part also facilitates the acquisition, retention, control and use of such property by respective Agencies.
Part 7 defines the various money laundering offences such as concealment, converting, disguising, and criminal property transfers. It also requires financial institutions, businesses and any individuals to report acts of money crimes to the UK Financial Intelligence Unit.

[148] FATF (2022), Anti-money laundering and counter-terrorist financing measures – United Kingdom 1st Regular Follow-up Report, FATF, Paris http://www.fatf-gafi.org/publications/mutualevaluations/documents/fur-united-kingdom2022.html
[149] Norton, S. (2018), "Suspicion of money laundering reporting obligations: auditor compliance, or sceptical failure to engage?", Critical Perspectives on Accounting, Vol. 50, pp. 56-66.
[150] A Suspicious Activity Report (SAR) is a tool prescribed by Bank Secrecy Act (BSA) of 1970. It is used for monitoring suspicious activities that would not ordinarily be flagged under any other reports.
[151] Norton, S. (2018), "Suspicion of money laundering reporting obligations: auditor compliance, or sceptical failure to engage?", Critical Perspectives on Accounting, Vol. 50, pp. 56-66.

Part 8 of POCA defines various legal processes such as confiscation, civil recovery, detained cash, money laundering and investigations of corruption. It also provides for powers to investigate, search and seizure, disclosing orders, and account monitoring orders.
Part 9 is meant for the purposes of deciding the recoverable amounts and the defendant's obligation to pay the ordered amounts.
Part 10 covers the disclosure of information, and usage of such information found during an investigation by any government agency. As an example, the Director General of the NCA in a civil recovery investigation can use any information obtained during criminal investigation.
Part 11 of POCA deals with enforcement matters and foreign warrants.
The Act also prescribes powers of investigators in case they probably think that the defendant is benefiting from a criminal lifestyle and how they should deal with such benefits of crime investigations.

Recently the following International Standards on Auditing (UK) relevant to money laundering were also promulgated:
ISA (UK) 315 which was amended in July 2020, is intended to serve as a strategic roadmap, guiding auditors to Identify and Assess the Risks of Material Misstatement by understanding the business of their client and the environment that it operates within. The standard required auditors to look into inherent risk factors such as subjectivity, change, complexity, uncertainty and susceptibility to misstatement due to management bias or fraud. The standard was effective from the on or after 15th December 2021.

ISA (UK) 240 which was revised in May 2021 defines fraud as deliberate in the misstatements of financial statements, and empowers the Auditor's to question such misstatements. It requires them to exercise professional scepticism and critical assessment of audit evidence given to them by their client. The auditors are empowered to seek explanations from the clients they auditing about the existence of the nature, terms, purpose, and involvement of any parties related to unusual suspect transactions.

ISA (UK) 250A revised in November 2019 and updated in May 2022. It provides for the auditor's responsibility to comply with other laws and regulations relating to the auditing process, excluding agreements binding the auditor to test and report separately on specific regulatory compliance issues. Whilst this standard prescribes this audit responsibility, it is imperative to note that auditors are not responsible for preventing non-compliance, they are also not supposed to detect non-compliance with all laws and regulations. The expectation is that they should ensure that the statements they audit are free from any forma of material misstatements.

ISA (UK) 250B, revised November 2019, prescribes the statutory rights and duties to report any suspect irregularities by the auditors to respective Regulating Bodies empowered by respective laws. This confirms the principles around audit quality and compliance to legal requirements.

ISA (UK) 330, also revised in July 2017 and updated in May 2022 to align with amendments effected in the revision of ISA (UK) 315 that has been effective since the 15th December 2017. It provides definitions of two types of audit procedures, substantive procedures and tests of controls. It requires Auditor's to respond to assessed risks in such a way that they create suitable solutions that deals with the risk of material misstatements with the intention to reduce the risk to an acceptably low level.

Recently the Financial Reporting Council (FRC) has called for submissions to a consulting process on strengthening and improve on both ISA (UK) 250A and ISA (UK) 250B to make

them more effective. In its consultation process, the FRC is proposing a more principles-based approach that will allow any significant information to be reported to respective regulators even where laws do not require it to be reported. The proposed standards reviews have raised many concerns, with some audit firms saying it represent unnecessary deviation from the international ISAs, and will increases the risk of confusion and inconsistent application. Some say it has a lot of requirements and thus increasing work-load. Taking into consideration the consultation process that has been undertaken, both standards are expected to be reviewed and effected after 15 December 2024.

In line with best practice, the UK government has not only made legislative changes but also engaged structural changes like merging the Assets Recovery Agency (ARA), which is tasked to freeze and seize proceeds of crime, with the Serious Organised Crime Agency (SOCA). The merger was provided for in the Serious Crime Act 2007 as amended by Serious Crime Act 2015. ARA's civil, recovery and taxation powers as per Proceeds of Crime Act 2002 were moved to SOCA, Revenue and Customs (RCPO) for coordination purposes.[152]

5.3 A COMPARISON WITH SOUTH AFRICA:

The ethical transgressions by Auditing Firms mentioned in this paper are not unique to South Africa only, the UK, EU countries, and the US of America experience almost similar major scandals.

As lessons learned, these scandals have pressurized countries like the UK to implement industry wide guidelines and international recognized best practices, whilst South Africa on one hand, is still lacking behind in implementing similar progressive and aggressive anti-money laundering strategies. In South Africa, like in the UK, the Treasury Department is in charge of the fight against money laundering. Both countries have endorsed global anti-laundering regulations to align with the global fight against money laundering efforts. The establishment of Economic Crime Strategic Board by the UK government, to determine a way forward in combating money laundering and to hold complicit corporations to account has been seen as a big success.[153]

South Africa has relied on internationally accepted standards (WEF, 2012:324)[154] in developing its strong auditing and reporting framework. The country endorsement of International Financial Reporting Standards (IFRS) issued by the IFRS Foundation and International Auditing Standards Board (IASB) has been accepted as a better option to follow. The intentions of the IFRS are to provide a common global accounting language. The successful implementation of these standards is also endorsed by the European Union. These successes are highly attributed largely to the effective implementation of King III code,[155] which is prescribed and recommended by South Africa's Companies Act 71 of 2008.[156]

The United Kingdom is also signatory to the Vienna Convention and the UN Convention against Transnational Organised Crime. It has included the principles of the Vienna Convention in its Criminal Justice Act whilst the UN Convention against Transnational Organised Crime forms part of its Serious Organised Crime and Police act. And just like South

[152] AML Legislation updates, "Assets Recovery Agency merges into SOCA" *BTC-Latest News* (Lancashire 04 April 2008)

[153] KPMG South Africa apologises for scandals, seeks second chance, Bloomberg, 10 December 2018. https://businesstech.co.za/news/business/290124/kpmg-south-africa-apologises-for-scandals-seeks-second-chance/ [accessed 23 August 2019].

[154] World Economic Forum: The Global Competitiveness Report 2011- 2012 http://www3.weforum.org/docs/WEF_GlobalCompetitivenessReport_2012-13.pdf

[155] Jansen van Vuuren, Schilschenk, J. 2013. *Perceptions and practice of King III in South African companies*. Institute of Directors SA. http://web.up.ac.za/sitefiles/file/2013_ALCRL%20King%20III%20Study%20Report.pdf

[156] Companies Act 71 of 2008. https://cdn.ymaws.com/www.iodsa.co.za/resource/collection/CB7E5DC1-E790-4BED-9693-9F8AA33E0032/Companies_Act_Guide.pdf

Africa, the UK is a member of Financial Action Task Force (FATF) and both countries have aligned their policies and legal framework with FATF Recommendations.

The UK has consolidated its money laundering crimes efforts in the Proceeds of Crime Act 2002 (POCA 2002) as amended by the Serious Organised Crime and Police Act 2005 (SOCPA) whilst in South Africa they are defined in the Prevention of Organised Crime Act 121 of 1998 (POCA 121 of 1998). The UK's POCA 2002 just like the SA's FIC Act and SA's POCA 121 of 1998 put the burden of responsibility to report suspect money laundering activities on the shoulders of auditing professionals and anyone who knows or is aware of any suspect activities to report them to respective government agencies.

The UK's Terrorism Act 2000 (TA2000)[157] serves the same purpose that the SA's POCDATARA[158] is intended to. Both Acts are meant to clampdown on any activities suspect of terrorism funding. The SA FIC Act 2001 further defines the duties and obligations of accounting people as far as money laundering controls are concerned whilst the UK's Money Laundering Regulations 2007 legally imposes a 'risk based' approach on firm's obligation to report suspect behavior. Failure to comply in both instances may give rise to civil suits. The South African POCA 121 of 1998 is also accountable for civil forfeiture procedures that prevent criminals from enjoying the benefits of laundering activities, whilst in the UK that function is delegated to SOCA through the Proceeds of Crime Act 2002 (PCA).

South Africa also established the two important anti-money laundering agencies, the Money Laundering Advisory Council (MLAC) and the Financial Intelligence Centre (FIC) as promulgated by the FIC Act 38 of 2001[159] to specifically deal with money laundering crimes. The FIC has been tasked with combating money laundering and financing of terrorism and protect the integrity of the country's financial systems. It is also tasked with dealing with identifying proceeds of crime.

Whilst the UK has a number of competent authorities and regulations tasked with the matter. AS an example, the UK Government in its attempt to strengthen its AML and anti-terrorist financing systems introduced the Oversight of Professional Body Anti-Money Laundering and Counter Terrorist Financing Supervision Regulations 2017. This gave rise to the establishment of the Office for Professional Body Anti-Money Laundering Supervision (OPBAS),[160] a watchdog charged with overseeing the AML supervisors. The OPBAS is tasked with improving cooperation between law enforcement Agencies and Private companies.

The continuous impact and value add of establishing these regulators can be recognised in many cases like the one about the breach of audit independence rules that happened in 2005, when a former PricewaterhouseCoopers auditor was fined £10,000 by the Financial Services Authority. A tribunal had ordered the penalty against Mr. Arif Mohammed who bought 15,000 shares of his audit client, Delta plc, at 80p each on 29 November 2002. Arif knowingly bought those shares after Delta had announced on the 9 December 2002 that it intended to dispose of its electrical division. He was found to have abused his position by cheating for personal gain after being privy to that information, and selling the shares at 105p the following day, making a profit of £3,750.

Mohammed, as an auditor, was aware that he was conflicted by dealing in Delta shares, thus undermined the integrity of the market by committing such a breach of trust. In defending his

[157] Home Office, UK. "User guide to operation of police powers under the Terrorism Act 2000 and subsequent legislation." Updated 14 March 2024.
[158] South African Protection of Constitutional Democracy Against Terrorist and Related Activities Act 33 of 2004
[159] SOUTH AFRICA. 2001. Financial Intelligence Centre Act 38 of 2001, Pretoria Government Printer.
[160] Financial Conduct Authority, "Office for Professional Body Anti-Money Laundering Supervision (OPBAS)"(London,23/01/2018)

actions, he claimed that while aware of the project, he was not privy to Delta's share price details, therefore his purchase was a genuine, lawful act with no intentions to commit any act of market abuse. He further argued that he considered the case to be more like a criminal offence, and therefore the FSA had to prove its case beyond reasonable doubt. But the FSA disagreed with him basing its case on a balance of probabilities, a fact which was confirmed by The Financial Services and Markets Tribunal.

In a case involving suspect to collusion recently, the UK's Financial Reporting Council (FRC) fined KPMG a record £21mn, reduced from £30mn, plus £5.3mn in costs, for their failures in auditing Carillion. These fines were for the audits they did for Carillion for the years 2014 to 2017. In 2017, the company announced expected provisions of £1.045 billion arising from expected losses on some of its contracts, and a goodwill impairment charge of £134 million. This announcement was made months after KPMG had given an unqualified audit opinion on the company's accounts. By the time Carillion went into liquidation, it had £29mn and liabilities of about £7bn.

These audit mishaps had provoked calls around the world to get Regulators to consider breaking up the Auditing Firms because the firms were suspect to collusion and were assumed to have excessive influence on corporate management. Further audit investigation were undertaken for KPMG audit reports that overlooked bribery and corruption offences done by Rolls-Royce between 2010 and 2013.[161]

Carillion's former chief executive Richard Howson was accused of misstating profits in relation to the company performance. He was fined £397,800 by Financial Conduct Authority as an individual and disqualified as a director of UK companies for 8 years, while his finance chiefs, Richard Adam and Zafar Khan were fined £318,000, and £154,000 respectively and barred from practising for 11 years as imposed under the Company Director Disqualification Act. The former partners of KPMG Peter Meehan was fined £350,000 and barred from practising for 10 years, and Darren Turner got cautioned for his involvement and was fined £70,000.

KPMG was accused by the Regulator of failing to collect sufficient evidence appropriate to the audit which would have enabled the auditors to conclude that the financial statements were a true and fair reflection of the business. In the 3 years that lead up to company's demise, it was clear that KPMG did not subjected it to rigorous, comprehensive, and reliable statutory audit processes. Their records were unreliable and, in some cases, misleading. It was alleged that the Auditors in some instances had assisted management to doctor financial documents to make them more audit friendly and had somehow assisted its 169 directors with hiding irregularities.

The ultimate fact was that the Auditor had failed to exercise his professional scepticism duties, and that the shoddy work he did was compounded by breaches of ethical standards relating to objectivity, independence, and integrity. This was evidenced by the fact that he did not complete some of the audit procedures until more than six weeks after the audit had been signed off. KPMG claimed that management had concealed information from the auditors.

Carillion's collapse impacted negatively on its employees, its pensioners, the local communities, investors, and taxpayers at large. Its collapse jeopardised the provision of school meals and the cleaning of hospitals. In February 2023, KPMG ultimately settled a £1.3bn lawsuit with the Insolvency Service, which had alleged that the auditing firm's pre-collapse

[161] Chloe Cornish, "Investigation launched into KPMG audit of Rolls-Royce" Financial Times (UK, MAY 4, 2017)

audit of Carillion was negligent. This collapse became a principal catalysts for reform of the audit sector in Britain. It led to the creation of a new regulatory watchdog, and a call demanding for the Big4 audit firms to "operationally separate" their audit and consulting arms.[162]

5.4 THE USA PERSPECTIVE:

The United States was first country to make an early effort to detect and prevent money laundering crimes. The country was one of the first nations to enact Bank Secrecy Act (BSA) in 1970 in its anti-money laundering legislation efforts. Like South Africa and the UK, the US has applied similar anti-money laundering principles in its legislation. And as a FATF member state, it has also been subjected to evaluations like all member states.

The March 2024 FATF mutual evaluation report on the United States has resolved that out of the 40 Recommendations, the United States was Compliant (C) on only 9, Non-Compliant on 3, Partially Compliant (PC) on 5, and Largely Compliant (LC) on 23 of the 40 FATF recommendations (Refer to the diagram below).[163]

There was much US improvement since its last 2016 Mutual Evaluation, FATF amended the following Recommendations 2, 5, 7, 8, 15, 18 and 21 on the US 2024 chart. Recommendations 2, 5 and 21 are now Compliant (C), whilst 7, 8, 15, 18 are now Largely Compliant (LC). With progress that the U.S. had made to address the technical compliance deficiencies that were identified in 2016, the country's Technical compliance rate was upgraded to 24 after rerating, which means it is now largely complying (LC). Considering the fact that the country still has three Immediate Outcomes remaining to be rated ME/LE for effectiveness, and nine Recommendations remaining rated PC/NC for technical compliance, FATF has kept it under enhanced follow-up.[164]

Other attempts that were made In the USA are that, in July 2002 the Government signed the so-called Sarbanes-Oxley Act[165] into law to regulate and govern all American Stock Exchange registered companies regardless of whether they are American or not. The aim of the Act is to increase corporate responsibility and transparency, protect investor interests, and enhance penalties for auditing transgressions. It is further meant to enhance auditor independence by minimizing conflict of interests between auditors and their clients.

A Public Company Accounting Oversight Board ('PCAOB') was established as per Section 101 of Title I of the Sarbanes-Oxley Act[166] to regulate registered public Accounting Firms and associated persons with an intention to protect the public interests and investor confidence in preparation of accurate audit reports.

[162] Mark Kleinman.2023. Former Carillion finance chief Khan handed 11-year boardroom ban. Sky News
[163] FATF (2024), Anti-money laundering and counter-terrorist financing measures – United States, 7th Enhanced Follow-up Report, FATF, Paris https://www.fatf-gafi.org/content/fatf-gafi/en/publications/Mutualevaluations/united-states-fur2024.html
[164] FATF (2024), Anti-money laundering and counter-terrorist financing measures – United States, 7th Enhanced Follow-up Report, FATF, Paris https://www.fatf-gafi.org/content/fatf-gafi/en/publications/Mutualevaluations/united-states-fur2024.html
[165] The full title of the Act is: The Corporate and Auditing Accountability, Responsibility and Transparency Act and Public Accounting Reform and Investor Protection Act, Public Law No 107-204.
[166] SOX 2002. Sarbanes-Oxley Act of 2002, Pub. L. 107-204, 116 Stat. 745. *SOX.* United States of America

USA Follow Up Report- 2024: Compliments of FATF 2024[167]

R.1 - Assessing risk & applying risk-based approach	R.2 - National cooperation and coordination	R.3 - Money laundering offence	R.4 - Confiscation and provisional measures	R.5 - Terrorist financing offence	R.6 - Targeted financial sanctions related to terrorism & terrorist financing	R.7 - Targeted financial sanctions related to proliferation	R.8 - Non-profit organisations
PC	C	LC	LC	C	LC	LC	LC

R.9 - Financial institution secrecy laws	R.10 - Customer due diligence	R.11 - Record keeping	R.12 - Politically exposed persons	R.13 - Correspondent banking	R.14 - Money or value transfer services	R.15 - New technologies	R.16 - Wire transfers
C	LC	LC	PC	LC	LC	LC	PC

R.17 - Reliance on third parties	R.18 - Internal controls and foreign branches and subsidiaries	R.19 - Higher-risk countries	R.20 - Reporting of suspicious transactions	R.21 - Tipping-off and confidentiality	R.22 - DNFBPs: Customer due diligence	R.23 - DNFBPs: Other measures	R.24 - Transparency and beneficial ownership of legal persons
LC	LC	LC	PC	C	NC	NC	LC

R.25 - Transparency and beneficial ownership of legal arrangements	R.26 - Regulation and supervision of financial institutions	R.27 - Powers of supervisors	R.28 - Regulation and supervision of DNFBPs	R.29 - Financial intelligence units	R.30 - Responsibilities of law enforcement and investigative authorities	R.31 - Powers of law enforcement and investigative authorities	R.32 - Cash couriers
PC	LC	C	NC	C	C	LC	C

R.33 - Statistics	R.34 - Guidance and feedback	R.35- Sanctions	R.36 - International instruments	R.37 - Mutual legal assistance	R.38 - Mutual legal assistance: freezing and confiscation	R.39 - Extradition	R.40 - Other forms of international cooperation
LC	LC	LC	LC	LC	LC	LC	C

C=Compliant; LC=Largely Compliant; PC=Partially Compliant; NC=Non-Compliant

Ratings:

Technical Compliance ratings which reflect the extent to which the Country has implemented the technical Requirements of FATF Recommendations.

Section 102 of Title I of the Sarbanes-Oxley Act defines responsibilities of the PCAOB to include the registering of public Accounting Firms.

Section 103 of Title I of the Sarbanes-Oxley Act defines the establishment of compliance standards regarding quality control, ethics and auditor independence.

Section 104 of Title I of the Act empowers the Regulator to do inspections of public Accounting Firms in order to ensure compliance with the Act, SEC rules and PCAOB.

Section 105 of Title I of the Sarbanes-Oxley Act defines procedural rules for conducting investigations and disciplinary procedures for Accounting Firms.

Section 103(*a*) (2) of the Act requires audit firms to archive for 7 years, audit-work papers and information that support their conclusions in a particular audit report.

Section 201-209 of Title II of the Act deals with eight sections concerning auditor independence.

Section 201(*a*) of the Act prescribes certain unrelated audit services, such as bookkeeping, outsourcing expert services, actuarial services, internal auditing or any advisory services which PCAOB prohibits public Accounting Firms from providing.

Section 201(*b*) of the act defines when exemptions to Section 201(a) can be given.

[167] Op sit

Section 203 of the Act prescribes auditor rotation every five years.
Section 205 of the Act prohibits previous employees that join audit firms to audit their previous employers.
Section 301 of the Act makes it mandatory of every listed company to have an audit committee.
Section 302 of the Act mandates CEOs and CFOs to certify the financial reports of their companies, indicating that the reports are accurate and fairly presented. Acknowledging legal responsibility for management's assessment of internal controls, and that the reports are risk-based.
Section 802 of the Act outlines penalties for noncompliance.

The Auditor's prime responsibility of identifying fraud related risks and the detection of misstatements in the financial statements must not be underestimated. Section 10A of the Securities Exchange Act of 1934 (SEA)[168] as amended, requires auditors to detection illegal acts that would have a direct and material effect on the determination of a client's financial statement during their auditing process. Therefore they play a crucial role during auditing, in that their role serve to protect investors by assuring them that the value of the audit and the related benefits thereof, will help as a verifier that they have assurance that the issued financial statements are free of any material misstatement.

Most US auditor's responsibilities are incorporated in the PCAOB Auditing Standards (AS), which prescribes and ensures auditing consistency meant to ensure that auditor's work is consistent across different audits and organizations including PCAOB's quality control standards.[169] This then clarifies important general principles required for an audit that includes reasonable audit assurance, professional care and scepticism, and professional judgment. PCAOB in accordance with Section 103 of the Sarbanes-Oxley Act of 2002, sets these auditing standards that summarize the specific rules that under Generally Accepted Auditing Standards (GAAS) must be followed by auditors when they audit a company's financial statements.

For an example:
AS 1001 defines independent Auditor's responsibilities and functions and distinguishes between Management and Auditor responsibilities.
AS 1301 refers to Auditor's responsibilities around communications most importantly about control deficiencies in an audit of Financial Statements.
AS 2301 concerns itself with the Auditor's responses to the risks of material misstatement.
AS 2401 informs the auditor of his responsibility for Consideration of Fraud in a Financial Statement Audit.
AS 2805 regards management representations to queries raised by auditors during the audit process.
AS 2901 refers to omitted procedures that require to be considered after the report date.
AS 2905 refers to subsequent discovery of facts that may exist at the date of the Auditor's Report.
AS 3101 refers to the processes involved when the Auditor has to expresses his Opinion about his Report on the audited Financial Statements.
AS 4101 refers to responsibilities regarding filings under Federal Securities Statutes. As example, section 11(a) of the Securities Act of 1933, as amended imposes a responsibility for false or misstatements of company financials to be reported.

[168] Securities Lawyer's Deskbook – Securities Exchange Act of 1934. University of Cincinnati College of Law. https://web.archive.org/web/20040610171913/http://www.law.uc.edu/CCL/34Act/
[169] The PwC Network adopted the IAASB's International Standard on Quality Management (ISQM) 1, Quality Management for Firms that Perform Audits or Reviews of Financial Statements, or Other Assurance or Related Services Engagements, as of December 15, 2022.

While these procedural standards are by no means exhaustive, they illustrate the unlimited auditor's responsibilities with respect to detections of fraud in regard an explicit requirement of a single law, in contrast to a multitude of laws meant to clamp down and discourage laundering crimes. It is therefore, important for professional auditors to understand the relationship between PCAOB Auditing Standards (AS) and any other auditing standards prescribed by other laws.

5.5 A COMPARISON WITH SOUTH AFRICA:

The United States of America, like the UK and South Africa, has applied similar anti-money laundering principles in its legislation. The SA, Auditing Profession Act No. 26 of 2005 (APA), focused solely on the regulation of the auditing profession, aiming on the introduction of a more robust framework to regulate the auditing profession and improve audit integrity. Section 45 of the APA deals with reportable irregularities and the investigation thereof. The same situation exist in the USA. Section 78j-l (B) of the US Code requires that suspicious matters, whether material or not, be investigated during auditing.

By probing such suspicious irregularities will also entails creating audit procedures meant to address the identified risks adequately (US's SAAS 240R paragraph 61). Section 303 (a) Title III (Corporate Responsibility) of the SOX also prohibits unlawful influence, coercion, manipulation or misleading of auditors by any officer or employee of a company intending to render the financial statements misleading.[170]

South Africa applies similar anti-money laundering principles in its legislation like the US, and complying with FATF audit standards. The country is also subjected to mutual evaluations like all member states. Its last assessment, led by staff of the International Monetary Fund, was done by FATF and the Eastern and Southern Africa Anti-Money Laundering Group in 2021. FATF adopted their assessment report at its June 2021 Plenary meeting.[171]

The report's conclusion was that South Africa had a solid regulatory regime for combating money laundering but still required to do some work on some of the non-compliance items just like in the USA report. Issues like international cooperation and matters around seizing and forfeiture of illicit assets obtained through criminal activities still needed to be worked on.

The evaluation reported that the country still needed to apply the risk-based approach by obligated entities and supervisors. Fortunately the country's Technical Compliance rate was upgraded to 24 after rerating. Based on technical compliance results, the country was placed in enhanced follow upon mode which can be termed 'increased monitoring' as it was still unsatisfactorily under performing in its compliance and thus rated non-compliant (NC), just like the USA.[172]Based on its compliance test, the country was rated 11 low or moderate. Since joining FATF, it only complied on 3 of the 40 Recommendations, 18 largely complying, 5 noncompliance, and 14 partial compliance. (Refer to the table below).

[170] Staub, E. 1978. Positive social behavior and morality: social and personal influences, New York Academic Press, 1(95):189-225.
[171] FATF (2021), Anti-money laundering and counter-terrorist financing measures – South Africa, Fourth Round Mutual Evaluation Report, FATF, Paris http://www.fatf-gafi.org/publications/mutualevaluations/documents/mer-south-africa-2021.html
[172] *Op sit*

South African Mutual Evaluation- 2021: Compliments of FATF[173]

R.1 - Assessing risk & applying risk-based approach	R.2 - National cooperation and coordination	R.3 - Money laundering offence	R.4 - Confiscation and provisional measures	R.5 - Terrorist financing offence	R.6 - Targeted financial sanctions related to terrorism & terrorist financing	R.7 - Targeted financial sanctions related to proliferation	R.8 - Non-profit organisations
PC	PC	LC	LC	PC	NC	PC	NC

R.9 - Financial institution secrecy laws	R.10 - Customer due diligence	R.11 - Record keeping	R.12 - Politically exposed persons	R.13 - Correspondent banking	R.14 - Money or value transfer services	R.15 - New technologies	R.16 - Wire transfers
LC	PC	LC	NC	LC	PC	NC	LC

R.17 - Reliance on third parties	R.18 - Internal controls and foreign branches and subsidiaries	R.19 - Higher-risk countries	R.20 - Reporting of suspicious transactions	R.21 - Tipping-off and confidentiality	R.22 - DNFBPs: Customer due diligence	R.23 - DNFBPs: Other measures	R.24 - Transparency and beneficial ownership of legal persons
NC	PC	LC	LC	C	PC	PC	PC

R.25 - Transparency and beneficial ownership of legal arrangements	R.26 - Regulation and supervision of financial institutions	R.27 - Powers of supervisors	R.28 - Regulation and supervision of DNFBPs	R.29 - Financial intelligence units	R.30 - Responsibilities of law enforcement and investigative authorities	R.31 - Powers of law enforcement and investigative authorities	R.32 - Cash couriers
PC	PC	PC	PC	LC	C	C	PC

R.33 - Statistics	R.34 - Guidance and feedback	R.35- Sanctions	R.36 - International instruments	R.37 - Mutual legal assistance	R.38 - Mutual legal assistance: freezing and confiscation	R.39 - Extradition	R.40 - Other forms of international cooperation
LC	LC	LC	LC	LC	LC	LC	LC

C=Compliant; LC=Largely Compliant; PC=Partially Compliant; NC=Non-Compliant

Ratings:
Technical Compliance ratings which reflect the extent to which the Country has implemented the technical Requirements of FATF Recommendations.

South Africa has since made significant progress. The country has passed Parliamentary Acts such as the Anti-Money Laundering and Combating Terrorism Financing Amendment Bill in August 2022. With the technical assistance offered by the US authorities to help the country exit the grey listing, and rebuild the capability of institutions combatting money laundering, the country is expected to do better in the next evaluation by FATF.

The impact of grey listing means an increase in the cost of raising finance and trading with global counterparties which could result in delayed transaction execution for businesses subject to additional requirements around sourcing of funding. Local banks could also experience increased customer screening requirements, as well as heightened levels of scrutiny and transactional costs.

[173] FATF (2021), Anti-money laundering and counter-terrorist financing measures – South Africa, Fourth Round Mutual Evaluation Report, FATF, Paris http://www.fatf-gafi.org/publications/mutualevaluations/documents/mer-south-africa-2021.html

The Lehman Brothers case[174] is a very prominent US money laundering case similar to that of the SA Gupta brother's case, in that it brought global economies tumbling down. Similarly coming from humble beginnings in German, the brothers started a small general store and ultimately turned their business into a huge mortgage origination business whose market value of $46 billion was wiped out when they filed for bankruptcy in 2008.

The Lehman Brothers case was larger than that of Enron, GM. Washington Mutual and World Com combined. They manipulated their financial books whilst their auditing firm, Ernst & Young looked the other way. As a result of bankruptcy, almost 30 000 people lost their jobs and millions of investors lost their money. Ernst & Young agreed to pay $10 million in a lawsuit settlement for overlooking Lehman Brothers accounting irregularities. It was clear in that scandal that the brothers betrayed both public and private trust in that they failed their fiduciary duties. Both countries have subsequently reviewed and assessed the effectiveness and proportionality of their regulatory regimes continuously, aligning them with industry's guidance rules and best global practices.

The WorldCom Case (a global telecommunication company) is another case of note regarding inflated revenues & assets that happened is the USA with similar sentiments to the South African Steinhoff case. The case was as a result of the 2002 WorldCom accounting scandal whereby the company allegedly got involved in fraudulently inflating its assets by nearly $11bn. The company's CEO, Bernie Ebbers recorded fake entries and thus inflated revenues. He also failed to accurately report line costs by capitalizing instead of expensing them.

The investigations revealed that WorldCom board of directors did not have the skills to protect the investors. It was revealed that they were affirmed to the Board by virtues of them being connected to the company's CEO, Mr. Ebbers. This led to the Boards' lack of transparency and accountability in financial reporting in their attempt to protect the CEO and the company. The corruption involved creation numerous schemes of fictitious cash flows and profits through cash flow manipulations that ranged from shifting, inflating, and boosting operation cash flow, whilst distorting and manipulating balance sheets and presenting misleading and overstated metrics (Schilit and Perler, 2010).[175]

The internal audit department discovered the scandal when they found nearly $3.8bn in fraudulent accounts, but they failed to report the true financial status of the company to the authorities as required by law or to the audit committee that also failed to meet on a regular basis. They claimed to be under capacitated, overworked and lacked the proper training and experience to can audit a fast growing entity like WorldCom (Ashraf, 2011).[176]

Arthur Anderson, the external auditors, were found to have put more value to their business relationship with WorldCom more than their compliance obligations. The investigations revealed that the auditors lacked professional competence, due diligence and independence of any influence by their clients. It was clearly revealed that they were influenced by top management to overlook and not report the accounting fraud that had happened, thus negligent on their part. They failed to detect early signs of the problems and continued to give a positive opinion about the company's financials (Schilit and Perler, 2010).

The failure in their obligation to exercise objectivity, independence and integrity, and their allowance of management influence, contributed to the worsening of the fraud and corruption scheme. The Auditing firm reached an agreement with WorldCom investors of paying $65

[174] Nick K. Lioudis, The collapse of Lehman Brothers: A case study, Investopedia(11 December 2017)
[175] Schilit, H. & Perler, J. (2010). Financial Shenanigans: How to detect accounting gimmicks & fraud in financial reports (3rd ed.). McGraw-Hill.
[176] Ashraf, J. (2011). The accounting Fraud at WorldCom. The Causes, The Characteristics, The Consequences, and The Lesson Learned. University of Central Florida Orlando, 1-54

million to resolve their class-action lawsuit filed in the wake of an $11 billion accounting scandal.

After this scandal, WorldCom filed for bankruptcy. The company's CEO was sentenced to 25 years in prison, for fraud, conspiracy and intentionally filing false documents. The company's bankruptcy resulted in over 30 000 getting retrenched and investors losing over $180bn. The Board of Directors were also charged with lack of corporate governance and lack of oversight.

The shocking collapse of Steinhoff International Holdings, a global retail company found with accounting irregularities in its books, saw its shares collapsing by 60% last year. Steinhoff lost more than R100-billion within 48 hours, almost the same amount the Guptas are accused of looting South Africa over a decade. Just like in the WorldCom case, Steinhoff management misrepresented its financials by hiding loses and inflating earnings. Deloitte was their auditors then and they were being investigated for overlooking these accounting processes irregularities. Ethical and effective leadership attempts by their board seemed inadequate since their influential Chief Executive who happened to sway auditors. As the scandalous events unravelled, he resigned, but was found guilty and fined. He killed himself.

5.6 TERRORISM FINANCING:

Terrorism Financing refers to direct or indirect provision of financial support to any person or group engaging in terrorism or related activity. There is a significant global increase in mobilisation of finances for terrorist activities by terrorist groups. Many of these groups are very well financed and this make it easy for them to can easily commit their acts of terror. There is a global effort by governments around the world working together with financial institutions, law enforcement agencies and many other formations in efforts to enhance existing laws intended to clamp down on terrorist actions and funding thereof.

Part 3 of the UK's Terrorism Act 2000 (TA2000) imposed the obligation and duty to report any suspect terrorism financing by accounting officers. After the USA September 11 debacle, the act was repealed and replaced by the Anti-Terrorism, Crime and Security Act[177] which expanded the obligations to report suspect activities and included the seize and forfeiture clauses by law enforcement agencies of any property acquired through suspect terrorism funding in the UK.

Part 1 and schedule 1 and 2 of the Anti-Terrorism, Crime and Security Act 2001 provides for freezing powers by treasury of any suspected illicit funds in order to prevent terrorist from accessing the accounts suspected of being opened to fund terror activities. These attempts to control terrorism funding are also reinforced in the Proceeds of Crime Act[178] and Serious Organised Crime and Police Act.[179]

The UK government also promulgated the new Money Laundering, Terrorist Financing and Transfer of Funds Regulations 2017, prescribing and compels firms to adopt greater risk based approaches to Anti Money Laundering (AML) and Countering the Financing of Terrorism (CFT). Whilst the South African government passed the Protection of Constitutional Democracy Against Terrorist and Related Activities Act 33 of 2004 (POCDATARA) which criminalizes commercial acts that are aimed at, or likely to, support the commission of terrorism and related activities. Any person can be regarded to commit a terrorist offence under POCDATARA if he knowingly engages in financing a suspect act and/or a person, or ought to

[177] Anti-Terrorism,Crime and Security Act 2001
[178] Proceeds of Crime Act 2002
[179] Serious Organised Crime and Police Act 2005

have reasonably suspected or known that the act will result in support for such activities or such persons.

The POCDATARA efforts are reinforced in the Financial Intelligence Centre Act 38 of 2001 (FIC Act) which creates an obligation to "accountable institutions" and "reporting institutions" to report suspicious and unusual transactions defined in the act.[180]

Furthermore, the SA's POCA 121 of 1998 gives guidelines on how to apply for notices on reasonable grounds that one is concerned in the commission of an offence or is associated with terrorist and related activities. This section should be read in tandem with the Protection of Constitutional Democracy against Terrorists and Related Activities Act 33 of 2004 (POCDATARA), whose main is to ensure that an Accountable Institution verifies that it is not transacting business with any known terrorist person or organization.

5.7 CONCLUSION:

It is very encouraging to witness the authoritative debates on global financial integrity during the G7 and G20 Summits, because it has dawned to the world that financial crimes have become global and borderless. And therefore the need to enhance global effectiveness in combatting financial criminal activities has become more than a necessity.

In 2015, a report from Global Financial Integrity, titled "*Illicit Financial Flows from Developing Countries: 2004-2013*," estimated that roughly USD 1.1 trillion, increasing at a rate of 6.5 percent per year on average, illegally find its way out of developing countries due to crime, corruption and tax evasion. To combat this outflow requires increased transparency, inter-agency co-operation, and international collaboration.[181]

Whilst lack of resources to combat the money laundering is a known matter, in the UK and SA, courts still appears to be too lenient to many Auditing Firms found to be flouting regulations as compared to the US where the Justice Department has made numerous efforts in prosecuting and fining a number of Auditing Firms and sent responsible accountants to prison.

The FRC has toughened its approach in its attempt to regulating audit in the UK in the wake of a series of high-profile UK accounting scandals involving some of Britain's largest firms. The aim was to restore the credibility of the audit professional, and enable the delivery of high-quality audit and assurance work. Although many Auditing Firms supports the FRC's objectives to maintain stakeholder confidence, whilst balancing the need to minimise the impact of regulatory requirement. A detailed review of proposed auditing standard requirements has raised serious concerns by Auditing Professionals that complained about an increase in the work load that the auditors are expected to do.

But the FRC has not backed down. It has been evident with new figures from Thomson Reuters Confirmation that the FRC has increased its investigations and dissing out huge punitive measures to non-complying firms and partners involved. The highest being the unprecedented KPMG's £21mn fine over its audit on Carillion in July 2022. This followed revelations that KPMG auditors had misled FRC investigators during spot inspections of Carillion audits and its outsourcing company, Regenersis.

This was followed by a sharp increase in the value of fines issued to UK's major auditors as a sign of a "show of force" intended to send a clear message to those not willing to comply. PwC

[180] Regulation Gazette as published in Government Gazette no 24176 (vol 450) dated 20 Dec 2002 available on the IRBA website.

[181] Spanjers Joseph, Kar Dev: "Illicit Financial Flows from Developing Countries: 2004-2013" Global Financial Integrity. December 8, 2015

and EY were also hit with fines worth multimillion-pound for the audits they did for London Capital & Finance (LCF) that was issuing bonds to prospective individuals. In December 2018, LFC was restricted to issue or approve further bonds. It went into administration in January 2019, owing about £237m to 11,625 individual bondholders.

The passing of the Sarbanes-Oxley Act by the US had a massive impact on corporate governance attempt to restore both local and international investor confidence in the US financial market, as it required all companies to implement new audit standards, increase transparency and accountability, and was meant to impose stricter and harsher punishment on any fraud perpetrators.

Several other policies and standards in regard to independency of auditors were proposed and implemented after the WorldCom debacle.[182] Lesson learned for future engagements by Auditing Firms is that they should maintain their independency as auditors at all times, refrain from their clients top management influence. Accordingly, it has also become urgent for multinationals to undertake new regulatory changes to strengthen transparency and consolidate the role of auditors in combatting money laundering.

[182] Bergen, L. (2005). The Sarbanes-Oxley Act (SOX) Act of 2002 and its effect on American Business. Financial services Forum Publication, Paper 17.

CHAPTER 6: Auditor's liability and the duty to detect.

6.1 INTRODUCTION:

According to PwC's 2018 Survey,[183] South Africa has experienced an increase even though not enough, in the rate of detecting and reporting economic crimes in the last decade. Seemingly auditors are still adamant to hold themselves as accountable and responsible as expected in identifying potential fraud and prevention of the recurrence of the previous mistakes that caused previous major scandals. The duty to Report suspicious and unusual transactions is widely regarded as an essential mechanism to proactively monitor suspect transactions linked to financial crimes, and the public relies to the auditing profession to be a watchdog capable detecting and reporting fraud in order to protect third party investments.

South African professional institutions are bound and obliged by various statutory regimes to report suspicious or unusual transactions and in return the Government has a duty to afford them protections as whistle blowers, a duty that is still being doubted, although the recommendations have been inculcated into various AML laws such as the Financial Intelligence Centre Act (FICA), and the Auditing Profession Act.

Legally the obligation to report suspicious irregular transactions is placed on anyone who knows or ought to have reasonably known or suspected that such irregular transactions is happening or have already happened. In terms of these rules a whistle blower does not have to present actual proof of a suspicious transaction, a mere reasonable suspicion is enough to report such. His suspicion ought to be based on his knowledge of the client's business, its financial history, background and behaviour. This obligation is placed on anyone including employees of a company, who ought to reasonably have known or suspected that illegal activity is or has happened, has a legal obligation to report such acts like corruption, theft, fraud, extortion, forgery, and any misstatements that they may be aware of, to respective authorities.

Therefore audit professionals are expected to make an attempt to detect and report suspicions of any criminal activity, including predicate offences whilst auditing companies. It should also be noted that professionals are not bound by any other laws or contractual obligations for reporting in good faith and are bound not to disclose to anyone that such criminality or predicate offence has been made.

This chapter intends to highlight the auditor's primary rights and duties as detailed in various laws. Most importantly the duty to report certain offences, making failure to report a criminal offence which could subject the individual Auditor of his Auditing firm to be delictually liable for damages that a third person could suffer as a result from their wrongful act of omission or commission, for which that third person is entitled to be compensated in terms of the law.

6.2 THE DUTY TO DETECT AND REPORT:

The Auditing Profession Act 2005 (APA)[184] and the Revised Guide on Reportable Irregularities issued by the IRBA, dated May 2015 ("the Guide")[185] set out the threshold for an auditor to lodge a reportable irregularity. In terms of the APA (2005), a registered auditor has a duty to report to the Regulator, if during the audit process he discovers any suspect irregularities that

[183] PWC's Global Economic Crime and Fraud Survey 2018
https://www.pwc.com/gx/en/news-room/docs/pwc-global-economic-crime-survey-report.pdf
[184] South Africa. 2005. Auditing Profession Act No. 26 of 2005. Cape Town: Government Printer
[185] Independent Regulatory Board for Auditors, 'Revised Guide for Registered Auditors: Reportable Irregularities in terms of the Auditing Profession Act," Revised Guide, May 2015

might have taken place or is about to take place. Failure to do that is regarded as a very criminal offense.
It is the auditor's duty to report any suspect act or omission where, based on his professional judgement, there is enough evidence that the act meets the definition of a reportable irregularity. Based on the information available at his disposal, the auditor would subsequently report the irregularity in good faith.

Section 1 of the APA defines a "reportable irregularity" as:

> *Meaning any unlawful act or omission committed by any person responsible for the management of an entity, which:*
>
> - *Can cause or is likely to cause material financial loss to the entity or any stakeholder.*
> - *Amounts to fraud or theft; or*
> - *Represents a material breach of any fiduciary duty owed to the entity or any stake holder.*[186]

The irregular reportable conduct in question, which might include fraudulent activities that entail sophisticated ways aimed at concealing illegally attained funds must be perpetrated by management or any employee holding an accountable position in the said company. However, it should be noted that not all unlawful conduct by management qualifies as a reportable irregularity. The inherent risk with fraud is that it may not be easily detected, even if due diligence and compliance with auditing standards was applied during the audit process. This means that commissioning an audit does not give a guarantee to the client that fraud will be detected. In many instances an auditor's knowledge and experience may not result in detection of fraud. An influential and experienced perpetrator, who is used to committing such illicit activities will do their best to cover their tracts.

According to the Association of Certified Fraud Examiners (ACFE) *2020 Report to The Nations—2020 Global Study on Occupational Fraud and Abuse*,[187] 43% of occupational frauds were detected through whistle blowers, 20% detected by Internal and external audit, and 12% through management reviews. 20% of those fraud cases were committed by owners and executives with a median loss of $600 000, and 42% of fraudsters were living above their means. The study estimates that a typical organization loses 5% of its revenues to fraud each year. The majority of these white-collar crimes are committed by directors and executives, could easily be found by auditors during audits of the financials if auditors could leverage technology and understand the rationalization used by other technologically astute professionals.[188]

South Africa, has expressed commitment to global anti-money laundering (AML) efforts like FATF recommendations. The Recommendations 20 and 21 expresses an obligation on its member state agencies to report suspicious or unusual transactions and protect whistle blowers respectively. Recommendation 20 recommends that professionals like Auditors who reasonably suspects any funds to be proceeds of criminal activities to promptly report their suspicions to relevant authorities. Whilst Recommendation 21 recommends that anyone that reports suspicious transactions in good faith should be protected from criminal and civil liability, and their identity should not be disclosed. Therefore, to ascertain whether an auditor has a

[186] South Africa. 2005. Auditing Profession Act No. 26 of 2005. Cape Town: Government Printer
[187] "Occupational Fraud 2024: A Report to the Nations. Copyright 2024 by the Association of Certified Fraud Examiners, Inc."
[188] Occupational Fraud 2024*: op sit*

binding obligation to detect and report fraud, one needs to first look at what South African laws prescribes.

Section 29 of the Financial Intelligence Centre Act, No 38 of 2001 (FICA), Section 44(2) of the Auditing Profession Act[189], and section 93 of the Companies Act 71 of 2008 details the auditor's primary rights and duties involved in auditing and examining financials before they can express their opinion on the fairness of those financials, and on whether those financials have been properly prepared. These Acts define how these duties are to be performed, and it is clear from these prescripts that an auditor has no statutory duty to detect fraud, but in case one suspect its existence, one is obliged to report it to the relevant authority. This is because audits are not designed to test controls, nor to catch fraud or detect every error. If audit processes prescribed in these Act are followed, the chances to identify any suspect fraud activities get maximized.

Auditing should be regarded as an exercise in sampling and materiality for someone primarily looking into more significant financial stuff to get an assessment of material exposure of the finances assuming to pick up misstatements if there are any, and give an opinion that could influence the decisions of users of those financial statements. To better explain this statement, two notable cases of *Pacific Acceptance Corporation v Forsyth* (1970)[190] and *Dairy Containers Ltd v NZI Bank Ltd* [1995][191] are authority cases when it comes to the duty to consider the possibility of fraud and reporting such. In both cases it was concluded that it is expected of an auditor to perform an audit in such a way that possible fraud and other irregularities can be detected. After identifying and assessing the risk of material misstatements, the auditor is expected to use his professional scepticism to address such anomalies to minimise the risk impact.

Common law, on the other side, prescribes the so-called *bonus paterfamilias,* easily explained in layman's terms as "a reasonable man standard" that an auditor must comply with. According to the standard, the duty to detect fraud can only exists if under similar circumstances, a reasonably competent and cautious auditor would have detected it and *vice a versa*.

Within the same compliance ecosystem, the Companies Act [192] requires Company Management to keep accurate business accounting records (section 28(1)); refrain from misrepresenting or misstating the said records (section 28 (3)); and present and explain correct transactional affairs and the financial position of business (section 29(1)(c)). This section 29(1)(c) must be read in tandem with section 104 to 106. Section 93(2) of the Companies Act also prescribes certain rights of the auditors, including the right to enforce these rights by applying to a court for an appropriate order. And Section 93(3) prohibits an appointed Auditor to perform any services for any company deemed to can potentially place that auditor in a position of conflict of interest.[193]

Section 45(1) of the Auditing Profession Act 2005 (APA) further broadens the auditor's obligation to report to respective parties, especially to the IRBA, with the overall aim of reducing white-collar crime, if he believes that a reportable irregularity by his client has occurred or is occurring. An auditor who submits such a report to the IRBA, must copy the company management as prescribed in sections 45(2) and 45(3) of the APA 2005, so as to

[189] Auditing Profession Act No. 26 of 2005 (APA)
[190] *Pacific Acceptance Corporation v Forsyth* (1970) 92 WN (NSW) 29
[191] *Dairy Containers Ltd v NZI Bank Ltd* [1995] 2 NZLR 30
[192] Companies Act 71 of 2008.
[193] APA *Op sit*

consider representations that management could make in respect of ratifying these assumptions made in the First Report in terms of section 45(3).[194]

After considering the management presentations, the auditors must review the First Report and submit a Second Report to the IRBA within 30 days, in which he indicates that either assumptions made in the First Report did not happen, or that adequate steps were taken to ratify the said assumptions, or in a worst scenario that the reportable assumptions are ongoing. In case the reportable irregularities are ongoing, the IRBA will provide copies of the reports made by the auditor to any appropriate and relevant regulators thereof. The IRBA will also take appropriate steps in line with promoting the integrity of the auditing profession in case of any allegations of improper conduct by auditors. Section 20(2)(f) of the APA empowers the Regulatory Board to enforce its code of conduct by investigating an auditor's conduct, appoint a disciplinary committee to conduct disciplinary proceedings, and impose relevant sanctions.

Section 46(3)(a) of the APA refers to the auditor's negligence prior to or at the date on which the audit report is signed.
Section 46(3)(a) of the Auditing Profession Act (2005).[195] Refers to the legal duty not to speak by auditors who are unaware of their negligence.

Any registered auditor who fails to report may be found guilty of an offense and fined or imprisoned According to Section 52(1)(a) of the Act. According to the section it is a crime for an auditor not to report a reportable irregularity (RI). Whilst Section 52(1)(b) prescribes that an auditor who "knowingly or recklessly" makes a report or a statement which is false in material respect, and subsequently expresses an opinion, shall be guilty of an offense.

The duties to report suspect anomalies when auditing financial statements of an entity are also the same in the USA. Paragraph 61 of SAAS 240R and Section 78j-l (B) of the US Code empowers auditors to investigate any suspicious anomalies during auditing processes with the ultimate aim of addressing the identified risks adequately.

In the UK, POCA 2002 and the Companies Act 2006, both Acts being amended, regulate statutory auditors who are required to review their relationships with clients continuously. In case they identify any suspicious irregular activity, they are obliged to report to the NCA by filing a Suspicious Activity Report (SAR)[196]. Contravention of these laws is punishable by a maximum prison sentence of 14 years and/or a fine.

The ambiguous Scottish case of *Royal Bank of Scotland v Bannerman* (2003)[197] caused alarm for the audit profession. It created a risk for auditors in that if they knew or were expected to have known that the bank was going to rely on their client's audited financial statements to approve any financial support to such client, and if it turns out that the statements were misstated, they owe a duty of care to a lending bank.

Section 327 of the UK's POCA 2002[198] (Not to be confused with SA's POCA 121 of 1998) prescribes offences as committed by people who conceals, disguises, transfers or removes illicit property which is suspected to be proceeds of crime from the jurisdiction where the crime was committed.

[194] APA *Op sit*
[195] *op sit*
[196] A Suspicious Activity Report (SAR) is a tool prescribed by Bank Secrecy Act (BSA) of 1970. It is used for monitoring suspicious activities that would not ordinarily be flagged under any other reports.
[197] *Royal Bank of Scotland v Bannerman Johnstone MaclaySC*2003 SC 125; 2003 SLT 181
[198] The Proceeds of Crime Act 2002 (as amended by the Crime and Courts Act 2013 and the Serious Crime Act 2015)

Section 328 of POCA 2002 states that a person commits an offence by getting involved in any way in an irregular action that they suspect or know that it will involve acquisition or use of criminal attained property.

Section 329 of the Act also provides that a person commits an offence if he knowingly acquires, uses or is in possession of property which represents the proceeds of crime.

Sections 393 (2), 495 and 498(1) of POCA does not require auditors to detect or investigate fraud however, the auditor is required to apply professional scepticism during audits with the intention to identify any misstatements if there is any, and report such if suspected as fraud.

In a classic South African case, *The State v Van Der Linde* (12331/12) [2016], the accused, Mr van der Linde, operated a fraudulent VAT scheme whilst acting as an employee of an accounting firm named: Ivan van der Linde and Associates. The accused masterminded a scheme to defraud SARS by supplying invoices substantiating false VAT refund claims, thus fraudulently claiming tax refunds for four companies during the period June 1997 to March 2005. He further laundered the proceeds of these funds by fund his exorbitant personal life style. The Ivan van der Linde and Associates firm was also not registered for VAT and was used as a conduit in perpetrating tax evasion crimes. The accused was found guilty of 255 counts of fraud, 1 count of forgery and 1 count of uttering and sentenced to imprisonment.[199]

In another classic case example of not reporting suspect funding, or being involved in generating such, is that of Mr. Vuyani Hako, the Chief Operations Officer Public Investment Corporation (PIC), a State owned Entity, which oversees close to R2.6 trillion in government employee pension funds. The confidential Audit Committee documents of the PIC revealed that five whistle blowers reported Mr Hako accusing him of nepotism and corruption before he was suspended in June 2022.[200]

The PIC instituted various investigations on him, including a lifestyle audit that uncovered suspicious transactions with transfers exceeding R4.5 million paid into Mr. Hako's home loan accounts with Rand Merchant Bank which were paid within two years, begining the month after he was appointed COO in December 2020 to Nov 2021 using money he could not adequately account for. When investigators questioned him about the payments, he could not explain the source of the funds. As such, investigators recommended that the PIC report a criminal case against Mr. Hako to the police in terms of AML laws considering the suspicious and unexplained transactions.

In Chapter 3 we discussed how KPMG got involved in assisting the Guptas to launder R30-million stolen Estina (a state dairy project) funds in Linkway Trading (a Gupta company) books, in order to fund a lavish Gupta family wedding in South Africa. KPMG overlooked the anomaly, and failed to act on their client in terms of the law,[201] instead they allowed for the classification of the wedding expenses as business expenses deductible for tax purposes. KPMG gave first priority to their relationship with the company since they were responsible for auditing and tax advisory services to Linkway Trading. This is the same company that invoiced a Dubai-based Gupta firm called Accurate Investments for R30-million for organising the extravagant

[199] S v Van Der Linde (12331/12) [2016] ZAGPJHC 179; [2016] 3 All SA 898 (GJ); 2016 (2) SACR 377 (GJ) (27 May 2016); South Gauteng High Court, Johannesburg
[200] Tawanda Karombo. *"Hako's R4.5m home loan settlement scandal raises more dust."* IOL (Johannesburg 19 Dec 2023)
[201] Section 45 of the Audit Profession Act (Act 26 of 2005),

wedding. Accurate Investments was found to be one of four UAE-based offshore companies owned by the Guptas' used as "laundromat" for illicit funds.[202]

Evidence led indicated that the KPMG firm allowed itself to be used by Linkway for the purpose of tax evasion. Linkway's annual financial report for the year 2014 misstated with the aim to evade taxes those millions lost due to the wedding exercise as "cost of sales." Given the public interest on the issue and the intention to safeguard the integrity of SARS, it would have been reasonably expected that a big firm like KPMG would undertake a thorough and careful investigation on the matter, instead it chose to overlook it. This evidence suggested that the firm, prioritised profit over professional duties and the county's laws.

This resulted in the IRBA charging KPMG with accessory in that they helped Linkway to evade tax. Subsequently in July 2018, Mr. Jacques Wessels, a senior partner at KPMG, was subjected to a disciplinary hearing by IRBA's around this matter. Six charges were meted against him, two of which involved dishonesty, three relating to negligence and one relating to a breach of auditor independence. In March 2019 the disciplinary committee recommended that Mr. Wessels be struck off the auditor's register as prescribed in Section 51(3)(a)(iv) of the Auditing Profession Act 26 of 2005 (the Act). The disciplinary committee further ordered him to pay part of IRBA's legal costs, and that his name and that of KPMG be published by public media, and IRBA to notify the South African Institute of Chartered Accountants (SAICA) of the findings and sanction.[203]

6.3 THE AUDITOR'S LEGAL LIABILITIES:

From the discussions above, it is clear that Auditors or Auditing Firms are legally bound by the laws of the countries they operate in. They are potentially liable for either or both criminal and civil offences or could even be exposed to regulatory investigations initiated by regulators in those countries, such as the Independent Regulatory Board of Auditors ("IRBA") in South Africa. The criminal liability occurs when an Auditor or Auditing Firm breaches that country's legislation and could therefore face prosecution in a criminal court for fraud and insider trading, or recklessly issuing an inappropriate audit opinion.

The civil liability occurs when third parties sue the auditor or the firm for negligence or breach of a duty of care resulting in such parties suffering some form of loss, or in a situation where an engaging client seek remedy for a breach of contractual obligations.

It is therefore important for auditors to understand the principles that establishes liability during delivery of their service, as well as ways in which they can limit such liability. An auditor is considered to be a professional accountant that is brought in to verify finances of a company and make sure that the financials are accurate. In case they suspect any anomalies with the figures, they investigate and report the anomalies to all interested stakeholders. There after they then "sign off" on the documents' accuracy, so they can bear some liability if the numbers are misleading.

They may not be held accountable for any misstatements of the financial statements if they can prove that they have done a very comprehensive audit that complies with auditing procedures and standards, that the audit reports were read by audit partners, vetted and validated by audit managers, and that the audit was conducted by experienced auditors.

[202] AmaBhungane and Scorpio, "The #GuptaLeaks: KPMG missed more money laundering red flags" Daily Maverick (Johannesburg, 27 November 2017)
[203] AmaBhungane and Scorpio, "The #GuptaLeaks: KPMG missed more money laundering red flags" Daily Maverick (Johannesburg, 27 November 2017)

Auditors can only be liable and face penalties if they breach their responsibilities to perform work with professional competence, due diligence and independent of any influence by their clients.

Auditors cannot be liable nor penalised if they can prove that they independently did the audit without any due influence or offers of bribes to falsify accounts. That the internal controls of the company were validated and any irregularities and system lapses were noted and highlighted in the audit letter to the Management. And if they can prove that in order to remove audit complacency, familiarity, and lack of independence with clients, audit principles were applied and complied with, and that they reported misstatements or suspicious activities to the relevant and respective parties.

It must be noted that the duty to report as enshrined in section 45 of the APA (2005) does not force the auditor to report suspicious misstatements first before investigating and verifying their suspicions, so that they can thereafter make conclusive decisions based on sufficient grounds, as to whether or not such misstatements or suspicious activities have taken or are taking place (IRBA, 2006: 25).[204]

Section46(2) of the APA (2005)[205] provides for a general limitation of liability for an auditor not to incur any liability to a client or third party in case they expressed an honest opinion in a report made during the auditing process, unless if the opinion was made maliciously, or negligently. This means that an auditor is afforded no legal protection for reporting an RI without sufficient grounds for doing so (IRBA, 2006: 25).[206]

Any liability due to breach of service contract, can only expose an auditor to regulatory investigations initiated by the (IRBA) which may lead to a disciplinary inquiry held against an auditor. These statutory investigations can also lead to search and seizure powers as granted to IRBA by the Auditing Profession Act.

Section 48 of the Auditing Professions Act, prescribes for IRBA to establish an investigating committee to investigate any improper conduct by auditors. After investigating the committee will recommend to the IRBA whether sufficient grounds exist for an auditor to answer to a charge of improper conduct in a disciplinary inquiry.

In terms of Section 49, the IRBA will after the investigating committee recommendations charge an auditor if sufficient grounds exist by first giving him an opportunity to enter into plea bargaining negotiations and plead guilty so that he can alternatively pay a fine in order to avoid a formal disciplinary hearing. It is also important to note that in June 2023 the Minister of Finance gazetted increased monetary fines for improper conduct of auditors from R200 000 to R5 million and for audit firms, the maximum fine is now set at R15 million. In case the matter goes to a disciplinary enquiry, an individual can be fined R10 million and an audit firm can be fined R25 million for improper conduct.

With all this in mind, it is important to note the following two interesting Supreme Court of Appeal (SCA) judicial decisions that had set authority with regard to the delictual liability of professionals to third parties in South Africa. These two decisions has changed the manner in which courts have to view an auditor's liability to third parties.[207]

[204] Independent Regulatory Board for Auditors: "Reportable Irregularities: A Guide for Registered Auditors," (issued 30 June 2006)
[205] South Africa. 2005. Auditing Profession Act No. 26 of 2005. Cape Town: Government Printer
[206] IRBA 2006 *op sit*
[207] S 1 of the Auditing Profession Act defines a "third party" as any person other than a client.

The first decision is in *Cape Empowerment Trust Limited v Fisher Hoffman Sithole.*[208] In which case it was discovered that Intella Group made a profit that did not exceed R10 millions for the period 1 March 1999 to 30 June 1999. The report would have revealed this deficiency if the auditor had performed his work appropriately. In that case Judge Brand JA concluded that:

> *"A misstatement in the auditor's report by the auditor was grossly negligent but not wrongful….."* [209]

In this case the auditor was given immunity from liability for misrepresentation of a misstatements in the audit report which was rendered "unusable" thereby defeating the purpose for the auditor's existence. It was wrong for an auditor to make such negligent misstatements in his audit report, however it is reasonably possible that the test for legal causation may render the auditor immune from liability since wrongfulness could not been established. [210]

The second decision was in *Axiam Holdings Ltd v Deloitte & Touche,* whereby Judge Navsa JA held that:

> *"An auditor may have a duty to warn a third party about the incorrectness of an audit report even if the auditor is unaware of its incorrectness, and ignorant to whom the warning must be made, if the third party can show that the auditor ought reasonably to have known of the incorrectness."*[211]

The meaning of this decision can be sourced from Section 46(3)(a) of the Auditing Profession Act which prescribes that though an auditor has a duty to speak, such a duty does not exist without a third party to speak to. The decision raises an unsettling representation by "silence" issue which could extend an auditor's liability to a third party beyond what may be the generally perceived boundaries.[212]It places the onus to prove that the auditor was negligent on the third party.

From this perspective, all that Axiam had to prove was Deloitte's negligence and the judge, based on evidence presented, agreed with them. The conclusion of the court was that the auditors foresaw the reasonable possibility of their conduct being harmful to Axiam, and ignored to take reasonable steps to ratify the situation. Deloitte was accused of failing to discover a bad debt valued at R29 million which was accounted for as goodwill and another irrecoverable debt worth R28 million. The auditor also did not verify a non-existent income of about R10 million which was accounted for incorrectly as a loan to a shareholder.[213]

These two court cases changed the basis upon which the auditor's delictual liability could be determined. For years it has been strongly assumed that a negligent auditor is a wrongful auditor. The two court cases changed those perception dramatically.

Section 46(3) (a) also covers the auditor's negligence prior to or at the time the audit report is signed. The section also "limits" the auditor's liability to third parties who can prove negligence in the Auditor's opinion, that it resulted in their loss, and that the auditor knew or could have reasonably known at that time that they would rely on the opinion.[214]

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[208] *Cape Empowerment Trust Limited v Fisher Hoffman Sithole* 2013 5 SA 183 (SCA) Maya, Cachalia, Shongwe JJA and Swain AJA concurring.
[209] *Cape Empowerment Trust Limited v Fisher Hoffman Sithole op sit.*
[210] Firer 'The auditor's liability for audited financial statements' 2019 *De Jure Law Journal* 468-485
[211] *Axiam Holdings Ltd v Deloitte & Touche* 2006 1 SA 237 (SCA) Howie P and Jafta J concurring.
[212] Jooste R "The Spectre of Indeterminate Liability Raises its Head" (2006) *SALJ* 563.
[213] *Bayer South Africa (Pty) Ltd v Frost* 1991 4 SA 559 (AD).
[214] *Delphisure Group Insurance Brokers Cape (Pty) Ltd v Dippenaar* 2010 5 SA 499 (SCA).

The circumstances to claim compensation for harm that has been suffered due to someone's blameworthy conduct, is a principle engaged in the South African law of delict.[215] This principle of extended *actio legis Aquiliae*[216] is allowed in South Africa and has since been affirmed in many subsequent cases. The *Aquilian* liability action is available to a plaintiff who can prove the elements mentioned above and the damages claimed should represent proper compensation for such loss.[217]Judge Corbett CJ in *Bayer South Africa (Pty) Ltd v Frost* case cautioned against the danger of limitless liability produced by the application of the extended *actio legis Aquiliae.*[218]

Judge Corbett CJ is quoted as having said that:

> *"[T]he duty of the Court (a) to decide whether on the particular facts of the case there rested on the defendant a legal duty not to make a misstatement to the plaintiff (or, to put it the other way, whether the making of the statement was in breach of this duty and, therefore, unlawful) and whether the defendant in the light of all the circumstances exercised reasonable care to ascertain the correctness of his statement; and (b) to give proper attention to the nature of the misstatement and the interpretation thereof, and to the question of causation."*[219]

The liability of South African auditors to third parties was recently reconsidered in a case; *Hlumisa Investment Holdings (RF) Ltd and Another v Kurkunus and Others [2020]*[220] by the Supreme Court of Appeal. As shareholders in African Bank Investment Ltd (Referred to in Chapter 3), the plaintiffs instituted action against *inter alia* Deloitte & Touché who were the auditors of African Bank Investment Limited entities for recovery of damages sustained as shareholders for denomination in their share value. The question to be addressed in this case was whether auditors of the Bank should be held liable to the shareholders of the Bank for losses they suffered as a result of the losses suffered by African Bank.[221]

The courts findings constituted application of existing principles on liability of auditors in general and on the auditor's legal duty in regard to pure economic loss. In addressing the liability question the court held:

- In case of negligent performance by auditors, the company is the proper Plaintiff to can sue for breach of contract, or breach of professional duties, or for any loss as auditors are accountable to the company in context of a contractual arrangement.
- That the purpose of the audit report is neither to protect the interest of investors, nor individual shareholders.[222]

As far as the auditor's legal duty in respect of pure economic loss is concerned, the court held that auditors have no duty to third parties (including individual shareholders) with whom no contract has been concluded unless specific factors may justify the existence of a legal duty.[223]

[215] Max Loubser, Rob Midgley, André Mukheibir, Liezel Niesing, & Devina Perumal. *The Law of Delict in South Africa.* Cape Town, Western Cape: Oxford University Press, 2009 (3rd edn. 2018).
[216] A legal action available to recover damages for the loss or destruction of property caused by someone else's fault.
[217] Op sit
[218] Bayer South Africa (Pty) Ltd. v Frost (105/89) [1991] ZASCA 85; 1991 (4) SA 559 (AD); [1991] 2 All SA 444 (A) (15 August 1991)
[219] *Bayer South Africa (Pty) Ltd v Frost* 1991 4 SA 559 (AD).
[220] *Hlumisa Investment Holdings (RF) Ltd and Another v Kurkunus and Others [2020] JOL 47567 (SCA)*
[221] Cilliers Wim, Clyde & Co, (2023); Exposure of auditors and accountants in South Africa. Camargue 28 August 2023 https://www.camargueum.co.za/exposure-of-auditors-and-accountants-in-south-africa/
[222] *Hlumisa Investment Holdings Op sit*
[223] *Hlumisa Investment Holdings Op sit*

In general, this meant that individual shareholders do not have a claim against auditors in case they make negligent misstatements concerning the companies' financial statements. Subsequently the Independent Regulatory Board for Auditors (IRBA) launched an investigating committee that investigated the complaint of potential improper conduct by the auditor in terms of Section 48 of the Auditing Professions Act. The regulator charged Deloitte's two senior managers, the deputy CEO Mgcinisihlalo Jordan, and another partner Danie Crowther, with misconduct relating to these signed off financial statements. It was argued that the audited financial statements were not "free of material misstatement", yet Deloitte partners expressed an unqualified opinion instead of a qualified one on them. They did not even emphasize the matter or include a disclaimer in the audit report. Mgcinisihlalo Jordan was fined R800 000 and suspended from practice for two years, Danie Crowther was exonerated from any charges.

Section 46(3)(b) of the Auditing Profession Act provides that If after issuing an audit opinion, and the financials had been represented to a third parties as a true reflections of the company affairs by an auditor who knowingly or could reasonably have known that these financial statements could influence the decisions of users, he or she will be liable for third party losses as a result of the reliance on the negligently given opinion.[224] In simple terms, the misrepresentation of the AFS to the third party, and the existence of the auditor knowledge that the third party would rely on the audited report are the deciding factors.[225] Both section 46(3)(a) and (b) provide oversight of the auditor's negligence.

The expectations in the UK and the US is almost the same as in SA. According to section 507 of the UK's Companies Act 2006, an auditor can be criminally charged if he is found to have knowingly, or recklessly caused a report (prescribed in Section 497) to be misleading, false or deceptive. The obligation to report is placed on a person who knowingly or ought to have known or suspected, regardless of the amount involved.

The duty to report is sufficiently dependant on a mere reasonable suspicion. This obligation to report is a fundamental global practice meant to strengthen member state laws intended to curb money laundering. Any professional that engages in or fails to report such a suspicious transaction is guilty of an offence and is liable to possible imprisonment. As far as civil prosecution is concerned, audit professionals can be charged under contract law and the law of tort.

In the USA, Section 103 of the Sarbanes-Oxley Act[226] regulate and govern all US Stock Exchange registered companies, and empowers the PCAOB to set Auditing Standards (AS) and Quality Control Standards that defines GAAS rules (issued by the Accounting Standards Board of the American Institute of Certified Public Accountants) to be followed by auditors. There is also Government Auditing Standards (GAS) issued by the U.S. Comptroller General, and the International Financial Reporting Standards issued by the International Accounting Standards Board. Section 10A of the Securities Exchange Act of 1934 (SEA)[227] as amended, prescribes detection of illegal acts requirements on auditors relating to the audit function. Even with all this safety net, the US 2019 statists on audit failures showed that 41% were due to failure to detect misstatement or disclosure errors, and 18% were due to Failure to detect theft or fraud. This trend has not slowed down but instead increased.[228]

[224] Section 46(3)(b) of the Auditing Profession Act 26 of 2005
[225] Neethling *Potgieter Visser Law of Delict* (2015), South African law 322
[226] The full title of the Act is: The Corporate and Auditing Accountability, Responsibility and Transparency Act and Public Accounting Reform and Investor Protection Act, Public Law No 107-204.
[227] Securities Lawyer's Deskbook – Securities Exchange Act of 1934. University of Cincinnati College of Law. https://web.archive.org/web/20040610171913/http://www.law.uc.edu/CCL/34Act/
[228] PCAOB 2019 inspection reports: Deloitte still tops; PwC deficiency rate rises again. By Maria L. Murphy. Compliance Week. Mon, Feb 8, 2021

Audit Professionals can minimize their legal liabilities by: doing a thorough due diligence of potential clients (Apply the KYC principle), always exercising professional Skepticism and avoiding illegal influences, ensuring that they are know the business of their clients, making sure that they sign a Liability Limitation Agreement (LLA) to prevent misunderstandings, and always doing a legal review on each audit engagement.

6.4 THE AUDIT FIRM'S LEGAL LIABILITIES:

The siege that has befallen Auditing Firms globally has diminished the trust that the audit profession has enjoyed over the years. In South Africa, Auditing Firms have been accused of shoddy deals with Gupta linked companies. Their auditors have been accused of unethical behaviour and thus subjected to disciplinary enquiries by the IRBA implicating the firms. Considering the fact that this accusations include chartered accountants, SAICA[229] and IRBA have launched separate enquiries on all these irregularities. The IRBA launched enquiries against implicated audit companies, whilst SAICA investigated individual practising members. Depending on the transgression, SAICA's disciplinary committees ordered penalties in the form of fines to permanent disqualification of individual membership, whilst IRBA could also impose fines and/or even withdraw audit firm's practicing licenses.

From a South African regulatory regime, the FICA (2001)[230] and the APA (2005) imposes a responsibility for IRBA to supervise compliance by all registered auditors in line with statutory laws of the country, take such action it deems necessary to remedy noncompliance. It is in line with these legal prescripts that IRBA accused KPMG of irregularities on the Gupta accounts, and for helping the Gupta family's laundering activities. Jacques Wessels, the lead audit partner at KPMG who represented the Audit Firm, denied the accusations but pleaded negligence, which he said does not amount to a serious offence of dishonesty. The charge sheet against the firm painted a picture of complicity in fraud. And because of the large scale paperwork that needs to be indulged, the matter still remains under investigation.

The other interesting case was the disciplinary hearing into Deloitte Africa's audit on African Bank, which was described as an unprecedented move by IRBA since the Audit Profession Act[231] permits for a disciplinary hearing to be held in public. This was the first, to have a hearing open to the public ever since in South Africa. It happened during a global crisis when regulators were under pressure to address auditing scandals involving the big four Auditing Firms: Deloitte, E&Y, KPMG and PwC. The shortcoming with such big hearings is that they take long considering the shortage of skilled staff to can thoroughly investigate these highly skilled audit firms, unlike in developed countries like the USA or UK. And the outcome of this case is also pending.

In comparison with developments in South Africa, the US Securities and Exchange Commission (SEC) pressed charges against KPMG SA, Deloitte & Touché and BDO for numerous audits they did circumventing the full oversight of the Public Company Accounting Oversight Board. The Companies paid penalties imposed on them. BDO Canada got a penalty of US$50,000, KPMG in South Africa paid $100,000 as a penalty for some of the irregularities, whilst Zimbabwe legs of Deloitte and KPMG agreed to pay disgorgement and interest totalling $99,057 and $141,305 respectively.[232]

Considering the current legal position of auditors in the UK, the Companies Act 2006 as well as UK-specific legal cases prescribes matters such as qualification and registration of statutory auditors, appointment and removal of company auditors. Auditors could also be criminally

[229] South African Institute of Chartered Accountants (SAICA)
[230] Section 44 read with section 45(2) of the Financial Intelligence Centre Act 38 of 2001
[231] the Auditing Profession Act 26 of 2005
[232] Iraj Abedian, "Audit profession needs a New Dawn"*Daily Maverick* (Johannesburg, 19 March 2018)

prosecuted under current UK laws for recklessly issuing an inappropriate audit opinion or for illegal acts such as fraud and insider trading (section 495 of Companies Act 2006), and for misstatements (section 507 of Companies Act 2006).

Similarly in the US, the Big Four audit firms have been fined billions of dollars for professional irregularities. Deloitte in 2005 settled a penalty of $250m for its audit of an insurance company named Fortress Re. PwC's settled a lawsuit by the shareholders of Tyco in 2007 for $229m. From a civil law perspective, the use of contract law and the law of tort are significant to the UK audit profession since they prescribe auditor liability to third parties. Contract law also allows parties to seek remedy for contractual breaches, as in the PwC settlement case to Tyco shareholders.

Under the law of tort, parties can seek remedy for audit negligence resulting in any loss if auditors can be found to have breached their duty of care. A case in example is the *Royal Bank of Scotland (RBS) vs Bannerman Johnstone MacLay* (Bannerman).[233] In this case RBS lost over £13m in unpaid overdraft facilities to an insolvent client APC Ltd. They claimed negligence by Bannerman as auditors in that they are alleged to have failed to detect a fraudulent and material misstatement in APC accounts. RBS had provided a loan facility on the basis of receiving APC Ltd's audited yearly financial statements. The Bank alleged that Bannerman knew about RBS's intention to use the audited financials as a basis for lending decisions. The court upheld that Bannerman owed RBS a duty of care.[234]

The Babcock's investigation is also another classic example alluding to the failure to gather enough support evidence and falsification of records by an auditing firm. The FRC hit PwC with a £7.5m fine which was reduced to £5.5m based on admission to failure by PwC over a string of serious breaches while auditing Babcock's accounts for 2017 and 2018.[235] The quality of the audits fell far short of the standards expected of statutory auditors. Evidence revealed that the Audit Firm failed to gather sufficient evidence to can challenge management to confirm their financial statements. PwC's auditors were also accused of creating a false documents as evidence for a sensitive government contract.

The misstatements in Babcock's financial statements were so glaring that a competent and cautious auditor would reasonably have detected them. The FRC accused PwC of lacking in competence, scepticism, care or diligence considering the fact that Babcock did highly sensitive UK government tenders worth billions of Pounds. The PwC team was also accused of failing to scrutinise a €640m (£570m) contract written entirely in French, not even attempting to get it translated. PwC was severely reprimanded and ordered to review and change its staff training programmes to address the shortcomings revealed, the got a fine of £7.5m reduced to £5.5m. FRC investigations on PwC audits on Babcock for audits done for 2019 and 2020 still continues and PwC might face further punitive fines.

Deducting from these experiences, Audit Firms can minimize their legal liabilities by ensuring quality control of their audits, assigning qualified and experienced personnel to conduct client audits, pursuing independence both in fact and in appearance, exercising due professional care, getting a letter of representation meant to remind the client about its primarily responsibility for a fair presentation of financial statements.

6.5 JOINT AND SEVERAL LIABILITIES:

Auditors can only be found liable if they are found to have breached their professional competence and due-care responsibilities. Therefore they may face individual penalties for

[233] *Royal Bank of Scotland v Bannerman Johnstone MaclaySC*2003 SC 125; 2003 SLT 181
[234] *Royal Bank of Scotland v Bannerman Johnstone MaclaySC*2003 SC 125; 2003 SLT 181
[235] Kalyeena Makortoff, PwC fined for Babcock audit failings including creating false record, 2023. The Guardian

their own failures and that third parties who have consequently suffered due to these breaches should be able to claim compensation.

Because penalties incurred by auditors have been unfairly increased high, the consequence of this fact brought about the civil law principle of 'joint and several liability' enforced in the UK and the USA. This means that in a case where multiple culpable parties are involved, an aggrieved third party seeking compensation for any consequential losses, may choose to pursue any one of those parties involved individually to recover the full loss, or may choose to sue all of them jointly for damages. In many instances pursuing the individual auditors may be a futile exercise, thus third parties in many instances prefer to pursue the asset rich audit firms for financial compensation since they also possess professional indemnity insurance for any negligence by their audit professionals.

In 2022 the Public Company Accounting Oversight Board (PCAOB) in the USA imposed a jointly $275,000 in total monetary penalties and other sanctions against KPMG and its two senior partners for supervisory failures and violations of PCAOB rules and standards in connection with the use of an unregistered accounting firm in Zimbabwe to perform audits of a public company between 2015 and 2017. Taking note of the fact that the U.S. Securities and Exchange Commission had opened an investigation against them, KPMG and the said two partners falsified KPMG Zimbabwe's recorded hours with the intention to reduce them by 77%. To protect investors, PCAOB held the audit firms and its partners liable for the shenanigans.

KPMG South Africa had also been fined $200,000 and ordered to improve its quality control policies and procedures. KPMG's engagement partner, Mr Cornelis Van Nieker was fined $50,000, which was reduced from $100,000 due to his plea of financial incapacity and was banned from joining any accounting firm. His co-accused, Mr. Coenraad Basson, KPMG's engagement and quality review partner was fined $25,000 and suspended from auditing service for one year.

As recent as early this year (2024) in the UK, EY and PwC were both fined £4.9m and £4.4m respectively for significant audit failures in the now-collapsed London Capital & Finance (LC&F). London Capital, a mini-bond firm was re-registered as a public company in November 2015. The company was selling high-risk, unregulated investments to retail investors that were promised returns of up to 8% a year, yet it had invested very little of that cash into safe interest-bearing investments. The rest of the money was invested into speculative property developments, oil exploration in the Faroe Islands and the purchase of a helicopter to be used by the executives.

The penalties came after the Financial Reporting Council's (FRC) investigation into how they breached fiduciary duties while auditing the firm's finances in the years leading up to 2019 when the company collapsed. By December 2018 the Financial Conduct Authority (FCA) had already imposed restrictions on London Capital's (LF&C) ability to issue further financial promotions before being placed under administration. The company was by then already owing about £237m to 11,625 individual bondholders. The regulator declared that the auditors failed to understand the business and allowed material misstatements in the company's accounts.

The seriousness of breaches in London Capital (LF&C) were made worse by the fact that their auditors were aware of the anomalies involved in LF&C which was selling unregulated financial products, and that potential investors relied on LF&C's clean audit opinions.

Another audit Firm, PwC and its audit engagement partner Jessica Miller, were also fined £7m and £150,000 respectively, for the audit they did for London Capital and Finance (LC&F) for the financial year 2015/2016. The Firm's Partner admitted to eight breaches, including failure to also adequately understand the nature of their client's business and its internal controls.

She also admitted to lack of applying sufficient professional skepticism during the audit. PwC settled early, reducing its sanction by 30%.

EY took over as LC&F's auditor in 2017 after PwC resigned but also failed to understand and properly scrutinize the business and the risk of fraud involved. In that financial year, LC&F increased its sales in bonds by a further £53.4m further exacerbating the risk. EY admitted to six breaches, including not understanding the risk of fraud and material misstatement involved and they were fined £7m. EY audit engagement partner, Neil Parker was fined £75,000 for his role in the audit of these financial statements. EY and Parker co-operated and admitted that their work fell short of audit standards and apologized. Fines were reduced by a further 10% after a 30% reduction for settling early.

Another auditor, Oliver Clive & Co, and its audit engagement partner Emma Benjamin, were fined £60,000 and £20,000 respectively in relation to LC&F failures that happened in 2015. The common element in all these audits was that the auditors failed to identify and assess the risks of material misstatement through understanding LC&F's business, and that they all knew about the risk the business was involved in considering the lavish lifestyles former LC&F executives lived.

In a similar South African situation, in February 2021, KPMG was blamed by VBS Mutual Bank Liquidators for negligence that saw the Bank ending up being looted. The Bank Liquidators alleged that the fraudulent ransacking of the bank's billions was due to the auditing firm not complying with the laws governing audits, and if the prescribed laws were followed, the auditors would have not missed the visible irregularities and would have reported to the relevant Authority. The subsequent fraud would have been prevented by the minister of finance placing the Bank under curatorship as prescribed by section 81 of the Mutual Banks Act 124[236], read with section 69 of the Banks Act 94 of 1990.[237]

What happened at VBS and LC&F was two complicated classic Ponzi schemes that took off modestly in the same year, 2015, and reached catastrophic proportions within a few years. The same business strategies were employed in both cases. Similarly the VBS bank took deposits from municipalities, and then embezzled that money to finance the lifestyles of a coterie of the bank's executives and their personal companies, their friends, and to a vast network of officials at about 20 local municipalities that needed to be bribed. At the time the bank collapsed, these local municipalities had a collective R1.5-billion unrecoverable cash stuck in the bank.

VBS ultimately ran out of money in 2018, and it was placed under curatorship. Its clients could not make withdrawals, until National Treasury came to the rescue with R260 879 594 available to pay clients up to R100 000 each. Those who had banked more than that were at a loss. At the last count VBS had lost about R2.7 billion.[238]

The Bank's liquidators pursued KPMG for more than R863-million owed to VBS by the Auditing Firm for their role in signing-off the March 2017 financial statement, which ratified a corruption scheme being perpetrated in VBS between 2017 and 2018. The Liquidators claimed a suspect R25 million was paid to a former KPMG employee, Mr. Sipho Malaba, who was the auditor that approved the alleged fraudulent statements. The payment was made through his two companies, Ihawu Lesizwe Trading and Betanologix. Malaba was instrumental in hiding the fraud from the authorities since as an audit partner to VBS, he allegedly clamped down on VBS's financial statements audits by hiding the fact that VBS had embezzled all of the cash it claimed to have for a fee. In total he took a bribe of R34-million through two front companies

[236] SOUTH AFRICA. 1998. Mutual Banks Act 124 of 1993, Pretoria; Government Printer.
[237] SOUTH AFRICA. 1990. Banks Act 94 of 1990. Pretoria: Government Printer.
[238] Lynley Donnelly, "KPMG woes deepen after VBS bank scandal" (Johannesburg, 15 Apr 2018)

for his efforts, an indication of how important he was. He has been recommended to the National Prosecuting Authority's Asset Forfeiture Unit for criminal litigation.[239]

VBS Board Members and the company Executives have also been accused of the alleged two-year looting spree totaling more than R2.3 billion and are also recommended for criminal litigation.[240] The investigations were still continuing during the research. KPMG subsequently agreed to pay R500 million to settle a three year lawsuit by VBS Mutual Bank liquidator. Former VBS chairperson Tshifhiwa Matodzi pleaded guilty to 33 charges as part of a plea bargain agreement. In July 2024 he was found guilty and sentenced to an effective 15 years imprisonment as part of the deal.

Given incidents mentioned above, it is clear that auditors have an important job to do. They are a very important and reliable asset to businesses because they are charged with ensuring the reliability of financial statements to be used by all stakeholders interested in such a business, which is why most of the time they find themselves caught in the middle of lawsuits in which they are claimed to have had errors of judgment, negligent and dishonest in opining inaccurate statements. Many lawsuits brought by third parties are unjustified, and audit firms are thus reminded that they are responsible for ensuring that their client's financial statements are presented fairly.

Auditors are therefore obligated to go about their daily business with due care, independent of any influence and exude competent Professionalism in order to avoid any lawsuit against them. They are expected at all times to possess requisite skills to complete their tasks in good faith and integrity, and should know that in case they be found to have been negligent, or acted in bad faith, or to have been dishonest, they can be either charged with criminal or civil liability. And whether exonerated or not, this can put a dark mark on their reputation.

It is also understandable that auditors are responsible to users of the financial statements like shareholders, potential investors and creditors of the company who use the financial statements that auditors are overseeing to make financial decisions. There are ways that could be used by audit firms to limit their exposure to claims of negligence. One way to limit exposure and help pay for representation is to invest in a professional liability insurance fund considering the costs that may be involved. This kind of insurance is a safeguard that can help auditors go through their legal hurdles by reducing financial exposure they may face during litigation and even trials.

The other way is to avoid being negligent in any terms, to stick to the terms and conditions of their engagement letter, and rigorously applying International Standards on Auditing, and comply with their Professional Code of Ethics. It is also important to include a disclaimer of liability to third parties in the wording of the audit report to avoid anomalies that were identified in a ruling in a UK case: *Royal Bank of Scotland v Bannerman* (2003).[241]

In the UK, Auditors are also permitted as per Section 534 of the Companies Act 2006 to enter into fair and reasonable Liability Limitation Agreement (LLA) during engagement. The agreement is meant to impose a cap on a compensation amount that can be claimed for negligence, breach of duty or breach of trust that could happen during auditing. The inclusion of LLA clauses in agreements has been debated a lot considering it is assumed to block any litigation by clients against audit firms who hide behind it for not producing good quality audits. These LLAs are also open to interpretation by the courts and in some instances the courts deviate on the caps agreed to depending on cost effects consequential of the said negligence.

[239] AmaBhungane and Scorpio, "VBS gang finally goes down: The Great Bank Heist" Daily Maverick (Johannesburg, June 17, 2020)
[240] Khaya Koko. "In a bizarre twist VBS liquidators sue KPMG for R863mn." Mail & Guardian (Johannesburg 24 FEBRUARY 2021)
[241] *Royal Bank of Scotland v Bannerman Johnstone MaclaySC*2003 SC 125; 2003 SLT 181

The UK government is increasing its efforts by introducing further audit reforms and undertaking a number of significant reviews. The promulgation of the revised suite of International Standards on Quality Management[242] aimed at improving quality management through risk assessment, and a revision of the ISA 220 (UK) Quality Management for an Audit of Financial Statements[243] based on the same titles that have been issued by the International Auditing and Assurance Standards Board (IAASB) are other efforts. The two reforms have brought about an improvement of the audit quality management process in the UK. The aim of these efforts have been to incorporate the management of audit quality throughout the whole firms, thus holding all employees and the Directors accountable.

In the USA, there is evidence that shareholder litigation against auditors has declined due to the brutally litigious environment. Even auditors' settlement pay-outs have fallen, but courts dismissals have increased. Some of the reasons for the declines is that audit quality has improved, the impact of the Supreme Court's narrowing of liability standards, the judgments against accounting firms and huge fines imposed on them has served as deterrent to shoddy work. Increased fines to audit companies such as the US$85.6 million judgment in 2014 against Deloitte & Touché in favour of the creditors of Livent, a theatre company. The impact of the judgment was such that it shifted the audit quality to improved levels and served as a deterrent to other firms.

Although there has been an increase in audit quality, one has noted and increase in unrestrained auditor liability exposure, a risk of bankruptcy of any of the Big-Four accounting firm. The audit services market has also experienced a reduction in competition. There is also a high turnover of professionals caused by the departure of experienced employees deserting the profession. The increase in audit fees, the financial reporting delays, and an increase in disclaimers and Liability Limitation Agreements has also impacted and created fears within the industry. The Securities Litigation Uniform Standards Act (SLUSA)[244] and the Private Securities Litigation Reform Act (PSLRA)[245], has reduced the liability exposure in federal securities law cases by introducing particularized pleading requirements and proportionate liability.

6.6 PROTECTION AFFORDED TO AUDITORS:

Although auditors are required to report suspect irregularities, and if they don't report they are subject to penalties and sanctions, the APA (2005) fails to address the protection of an Auditor in case of a mistaken belief, after the auditor had reported a suspect act which after investigation is discovered not to be a reportable matter. Although Section 46(2) of the APA (2005) prescribes that unless an auditor's opinion is malicious, fraudulent, or negligent, the auditor cannot be held liable to a third party or his client in respect of such an opinion been made in the ordinary course of his duties. This is a clear indication that there is no solid legal protection afforded to auditors for reporting a RI without sufficient grounds (IRBA, 2015).[246]

Section 29 of FICA imposes a general duty on all businesses, and every employee, to report to FIC[247] on any suspected transactions involving proceeds of crime or tax evasion. Unlike section 45 of the APA (2005), reporting under section 29 of FICA gives a limited defence relief

[242] International Standard on Auditing (UK) 220 (Revised July 2021) (Updated March 2023), (ISA (UK) 220), Quality Management for an Audit of Financial Statements, also becomes effective from that date.
[243] The International Standard on Quality Management (ISQM) 1, quality management for firms that perform audits or reviews of financial statements, or other assurance or related services engagements
[244] The Securities Litigation Uniform Standards Act of 1998 (SLUSA), Pub. L. Tooltip Public Law (United States) 105–353 (text) (PDF), 112 Stat. 3227,
[245] Pritchard, Adam C. "The Screening Effect of the Private Securities Litigation Reform Act." S. J. Choi and K. K. Nelson, co-authors. J. Empirical Legal Stud. 6, no. 1 (2009): 35-68.
[246] Independent Regulatory Board for Auditors, 'Revised Guide for Registered Auditors: Reportable Irregularities in terms of the Auditing Profession Act," Revised Guide, May 2015
[247] The FIC entity was established by the FIC Act 38 of 2001 and reports to the Minister of Finance and to Parliament.

to an auditor who has been associated with money laundering activities by default, but subsequently reports the suspect activities. This does not give the auditor immunity from being charged for any other offenses or does not provide a defence against delictual or contractual claims against the auditor for incorrectly submitting a report to the FIC (section 7(a) of POCA). The FICA or POCA prescriptions therefore indicate that even if the auditor reported a transgression, suggestions are such that the reporting obligation would be established by the APA (2005).

Fact is, the auditor's genuine aim and the legal duty to report without delay, compared to current practice could expose auditors to litigation risk. The status quo, creates a dilemma that contradicts the basic tenets of fairness and the duty to report in the interest of the public. The biggest challenge for Auditors is that most of the wealthy multinationals are audited by the Big Four accountants and it is not in their best interest nor of the powerful to point out when something goes wrong. Auditors are faced with a dilemma to report or not to, and failure to report promptly can subject them to fines, professional suspension or imprisonment (IRBA, 2015; section 51 of the APA 2005). Despite the statutory duty to report, auditors who report prematurely can still be subjected to civil claims without statutory protection, even if they had reported in good faith. With this lack of adequate protection comes fear of reprisal, thus the legitimacy of whistle-blowing becomes questionable.

Considering the above limitations, the only defence could only be mounted under common law, where an auditor is possibly subjected to a delictual claim for damages suffered by the client or a third party. The other possible claim could be for breach of contract, subject to contractual terms agreed and signed between the auditor and the client. In the case of a delictual claim the onus of proof rests with the claimant who must prove auditor conduct in terms of wrongfulness, fault, negligence and damage. A defendant who faces a civil claim can also rely on a common law statutory defence that authorises the infringement of the rights of others, and the onus of proving such rests with the defendant to prove that causing the harm was within the limits of legal statutes.

Looking at the VBS Mutual Bank's case that has been discussed earlier, in which VBS liquidators sued KPMG for more than R863-million, blaming the auditing firm over shoddy auditing of the Bank's books and negligence that resulted in the alleged looting of the bank's billions by its senior employees. Taking into consideration the collusion by a former KPMG auditor, Sipho Malaba who was bribed with more than R25-million to overlook and approve the alleged fraudulent Bank statements. Malaba could not expect protection since instead of reporting he colluded with the criminal activities engaged by the Bank.

The liquidators claim that the fact that the Audit Firm ignored reporting Malaba's apparent conflict of interest makes KPMG to be liable. They emphasise that, had the auditor conducted his work in line with the laws governing audits, they would have identified the fraud being committed and would have devised strategies to prevent it and reported the matter to the registrar of banks, who In return would have had VBS placed under curatorship. After these revelations KPMG agreed to pay R500 million as a settlement with the liquidators.

In contrast, the situation in the USA is such that the promulgated Whistle Blower Protection Enhancement Act of 2012 and Sections 302 and 806 of SOX (2002)[248] prescribes protect measures for the whistle blower who might fear of reprisal and the whistle blowing process itself. Furthermore the SAS 54 limits the need to report irregularities to a third parties unless when subpoenaed to do so, or if compelled by the Securities and Exchange Commission.

[248] Staub, E. 1978. Positive social behavior and morality: social and personal influences, New York Academic Press, 1(95):189-225.

This view is confirmed by the *SAS 99: Consideration of Fraud in a Financial Statement Audit* (AICPA, 2002) and the Private Securities Litigation Reform Act of 1995 which imposes the duty to report illegal acts to the Securities Exchange Commission. The Act also introduced the principles of proportionate liability, as opposed to joint and several liability, and it provides protection from civil liability claims for auditors who report in good faith.

In the UK, the Professional Standards (SAS 110) requires auditors to report suspect activities for purposes of public interest, irrespective of client confidentiality as long as they act *bona fide*, and thus cannot be held liable in any form. The Public Interest Disclosure Act 1998 (PIDA) also places the burden to report suspect activities or irregularities on all employees. These UK laws offer a measure of protection for the auditor against civil claims such as defamation or breach of professional confidentiality.

In April 2020 Ernst &Young Global Ltd was ordered by English High Court judge to pay Amjad Rihan, one of EY's youngest partners at the age of 36, US$11 million in a classic case where he became the first employee to ever sue a big accounting firm for expelling him after he had exposed a string of reportable irregularities by a client based in Dubai and the subsequent cover-up by the auditing firm. According to the court's findings, the firm obscured audit findings and helped their client, Kaloti Jewellery International to launder money and hide suspected illicit exports.

Another EY scandal expected to be one big scandal of the FTSE 100 in a decade, is that of an Abu Dhabi based hospital group named NMC Health PLC listed in London. The group's board included former partners of EY as members, evident of the existence of a cordial relationship and an "information asymmetry" between the company and its auditor. Investigators tried to find out how NMC's US$4 billion of undisclosed debts went undetected, potentially exposing EY to allegations of negligence after it had earned £14 million for NMC audits over seven years.

These scandals have hit hard on the efficacy of EY's global business model since the services agreements were signed off in London. This impact on the audit firm's global models was also felt by firms like KPMG whose brand suffered global knock down when in South Africa, most of its clients terminated their contracts with them, and firm suffered high turnover of skilled staff for its involvement in corruption scandals. PwC was also being investigated in the U.K. for alleged misconduct by its Italian office on audit work done for telecoms company BT.

6.7 CONCLUSION:

To conclude, the obligation to report to respective authorities, any RI committed by a client as defined in Section 45(1) of the APA,[249] whether such RI is material or not, is intended to reduce white-collar crime in companies. This requirements is in recognition that if not reported, such irregularity can have serious consequences for the company and any interested parties.

Although it is impossible to guard against any liability claims for professional negligence that an auditor may incur, indications are such that good reporting, quality auditing, scepticism, and understanding of the client's business may create a conducive environment for auditors to play a critical role in detecting and reporting financial irregularities to respective authorities.

[249] Auditing Profession Act No. 26 of 2005. Cape Town: Government Printer

Wrongfulness, accountability and liability was established in the *Cape Empowerment Trust Limited v Fisher Hoffman Sithole.*[250] It was also established that the community expects auditors not to make mistakes with financial statements since third parties rely on the information, and that they expect auditors to be held liable for errors of judgment and negligent inaccurate statements.

The essence of the court's decision in the *Axiam Holdings Ltd v Deloitte & Touche*,[251] was not about auditor negligence and reported misstatements, but it was about auditor's failure to warn Axiam as to the errors in the Audited Financial. The auditor had actual foreseeable knowledge that his client relied on the correctness of the audit results. The case was also about auditors having a duty to speak even in the absence of someone to speak to. This has left a prospect of indeterminate liability which should have been curbed by correctly interpreting Section 46(3)(b) of the Auditing Profession Act, which eliminates such potential liability and limits such to a specific defendant in specific circumstances. That makes one to can conclude that there is a clear indication that there's a need for auditors to take responsibility for the accuracy of their audited Financials to the third party.

The Bannerman[252] case brought some relief to auditors, it did not entirely eliminate auditor liabilities to affected parties, but it reduced the assumed liability scope for courts on auditors. Whilst critics of the case believe that it devalued audit reporting. The critics further argued that the disclaimer reduced the pressure to perform good quality audits, acted as a barrier to litigation for negligence, and reduced the credibility of the audit report in the eyes of the user.

This Chapter was more about auditor's primary rights and duty to report as detailed in the Auditing Profession Act, and a detailed discussion about the two Supreme Court of Appeal (SCA) judicial decisions that got auditors to be unsettled was made mention of. Details of what each case means to the Audit Profession was also discussed. We also discussed how, a South African auditor who mistakenly reports irregularities in good faith, can be subjected to a disciplinary inquiry, or huge fines and penalties, should he choose not to report as is required by section 45 of the APA (2005), and yet the same law affords him no protection. Similarly, the whole AML regulatory regime offers no practical protection for such to an auditor.

[250] *Cape Empowerment Trust Limited v Fisher Hoffman Sithole* 2013 5 SA 183 (SCA) Maya, Cachalia, Shongwe JJA and Swain AJA concurring.
[251] *Axiam Holdings Ltd v Deloitte & Touche* 2006 1 SA 237 (SCA) Howie P and Jafta J concurring.
[252] *Royal Bank of Scotland v Bannerman Johnstone MaclaySC*2003 SC 125; 2003 SLT 181

CHAPTER7: The impact of Money Laundering activities.

7.1 INTRODUCTION:

Money Laundering has gone multinational and enterprising, and like any other criminal enterprise, it is a trillion-dollar organized business that collects its own taxes and enforces its own rules. It has taken advantage of globalization, weak enforcement, and the use of modern technology to replicate the appearance of legitimate businesses around the world. The world's great and well organized crime syndicates like Italy's Mafia, drug cartels, Japan's Yakuza, Chinese triads, and the Russian mob to mention a few, have been hard at it trying to clean as much as they could of illicit cash they accumulate through criminal activities. They use multiple bank accounts, shell companies, fake invoices, and tax evasion systems and many other methods to try and clean their money.

These syndicates have been on it for centuries and are still going strong seeking to control economies, natural resources, and the people in their sphere of influence. Their global networks continue to undermine democracies and affect lives whilst destroying world economies. They often bribe politicians, bankers, auditors, government and security agency officials as a relatively direct way to penetrate finance structures. The officials bribed often act as accomplices in these criminal acts, thus making these crimes go on for a very long period. They also donate large sums of money to party political campaigns as one of the means used to gain influence over politicians. This emphasises suspicions that state corruption can facilitate organised crimes and materialise at various institutional levels.

Circumstantial evidence tends to confirm that there is deep interdependent links between exploits of organised crime and corruption in the politics of most developing countries, undermining the stability of these countries, their governance, and their democratic structures. The assumption is that there's commonality of characters between political state capture by criminal networks and general corruption in countries identified with high levels of organised crime. The symbiosis fostered between the state and criminal organisations which is meant to increase social instigating and political unrest within the societies is so apparent.

The number of incidences of public treasury looting, and money laundering by government officials and criminal syndicates globally is so alarming, but as fast as they become public knowledge they also fizz off without convictions because of influences in high places. Which increases the suspicions and allegations about collusion between certain professionals, government officials and the judiciary being bought to write off these cases.

The signing of the United Nations Convention against Transnational Organized Crime in December 2000 in Palermo, Italy was a significant development in an effort to promote international cooperation against money laundering. This was a demonstration by global community that they recognised the fact that they must work together to effectively address and fight cross-border financial crimes that has a destructive impact on economies and socio political facets of every nation.

The recent developments to combat money laundering has revealed that countries with weak reporting infrastructure and auditing processes gets to be an easy target that becomes a fertile ground for corruption and money laundering. There is a need therefore by Governments across the world to enforce transparency and integrity in financial audit reporting. The lack of transparency and self-discipline by auditors is a threat to the global economic stability.

The United States and UK have made various efforts to introduce some regulatory frameworks to protect the world's financial systems from criminality by applying targeted and comprehensive sanctions to individuals, transnational companies, and national jurisdictions that violate AML principles. In the UK, the National Crime Agency ('NCA') has cautioned overseas companies, some of whom are currently the subject of a criminal investigations, for being used as tax avoidance vehicles used to launder illicit funds in UK by procuring property for criminal or illegitimate purposes.[253]

Furthermore the UK Government introduced regulatory regimes such as the Money Laundering and Terrorist Financing (Amendment) Regulations 2019[254] and the Unexplained Wealth Orders (UWOs).[255] UWO is a court order issued by courts compelling the suspected target to reveal the sources of their unexplained suspect proceeds. The UWO is used as one of the tools adopted to fight against money laundering in the UK. These orders give authorities the power to seize assets that cannot be explained as acquired by legitimate means. Whilst Regulations 2019 requires firms to undertake more stringent due diligence checks of their clients and to report suspicious client activities to the authorities.

The introduction and use of AI technology to combat money laundering has also become a new trend in analysing large amounts of data and identifying suspicious activity trends and patterns. Embracing technology has assisted in the better detection and prevention of money laundering activities.

The main focus of this section is to reflect on the disposition by financial crimes of the South Africa's economy, the country's social existence, and its political stability, focusing mostly on the government efficiency and the community at large. We will dwell into the impact that money laundering has with regard to activities such as tax-base erosion on a country's economy, its impact on inflation, its governance systems and its reputational risk, and lastly on its effects on the society at large.

7.2 THE ECONOMIC EFFECTS:

Accepting the notion that money laundering is a global outstanding crime that is made up of illicit funds flowing across borders of various countries, developing countries gets to be more exposed to its exploits as a result of the nature of their unregulated economies that are conducive to carry out illicit activities. As a result its globalized impact poses grave threats to economic stability, worldwide security and has a tendency to can destabilise a multitude of economies through injection of illicit funds into legitimate financial systems. The entry of these illicit funds can easily distort market mechanisms thus lead to economic imbalances and crises. This injection finally erodes the value of legitimate funds in the system and can also be used in financing criminal activities such as terrorism and thus undermine global security. It is from this basis that the global cooperation and coordination to combat money laundering requires a concerted joint effort by all nations.

The compromise and the after-effect that laundering brings to the integrity and stability of institutions like Banks, can also result in loss of confidence and trust in these institutions, and thus result in a decrease in the use of banking services by communities, leading to reputational damage of the institutions, an increase in regulatory scrutiny, and potential systemic risks. In extreme cases, it can trigger financial panics. Because it involves illegal activities such as organized crimes, drug trafficking and corruption. Such activities can distort the normal functioning of markets, affecting competition, pricing, and resource allocation.

[253] NCA, 'National Strategic Assessment of Serious and Organised Crime 2018'

[254] The Money Laundering and Terrorist Financing (Amendment) Regulations 2019 No. 1511 have been published and may be found here – http://www.legislation.gov.uk/id/uksi/2019/1511.

[255] Brun Jean-Pierre, et al. 2023; *Unexplained Wealth Orders: Toward a New Frontier in Asset Recovery*, Published by StAr.

As an example, one classic case that triggered financial panic is that of VBS which could be called an industrial-scale looting exercise by 53 individuals including the bank executives who paid for luxury cars, multiple properties and financing of their personal companies to the tune of R2.7 billion.[256]

The Bank served tens of thousands of ordinary clients, many of whom were poor and working-class people in Limpopo Province at the time of its implosion. It was placed under curatorship in March 2018 because of its liquidity crisis, and by November same year the High Court granted its final liquidation order. Its many clients hoped that the bank could still be saved considering the amounts they had deposited into the Bank, but those hopes were dashed by the final liquidation order. Unfortunately the bank was looted into insolvency and could not be saved. Individual clients and small retail depositors who had saved over R100 000 with VBS could only recover up to R100 000 as relief offered by Government, anything else was a loss.

The after effect was that most people lost their confidence in the financial institutions. They reverted to their life of poverty after losing their savings that were envisaged to be used to open businesses or buy properties and sustain their living. Their economic stability and security was left shaken, some even died out of shock.

Some of the looted cash was used by Bank officials as bribes for those who were responsible for oversight such as auditors, to look the other way. Some was used to bribe municipal officials for unlawfully placing municipal deposits to the value of R1.6 billion with VBS which was all lost. The question that remained was: How could auditors not detect these conspicuous irregularities? And the only answer one could get to was that they colluded with the criminals. And the worrying reality is that some of the alleged criminals ended up being elected to the South African Parliament before they could even be prosecuted.[257]

The social impact of the VBS scandal was such that more than 300 of its clients that had more than R100 000 cash balance were small savings clubs, burial societies and stokvels. 16 of those had their members relying on those savings for a range of potential projects and some like burial societies depended on their cash in case of urgent needs like family deaths to access their money, some saved to build homes for their families, some saved for their children University education which could not happen anymore, they lost it all.[258]

The tricky issue about money laundering is that it is not that easy to quantify since it is an illicit activity for which no precise transactional records exist**.** It is therefore difficult for researchers to quantify its negative economic effects on economic development at country level. According to the United Nations Office on Drugs and Crime, it is speculated that between $800 billion and $2 trillion is laundered each year, which amounts to 2-5% of global GDP.[259]

This is a justifiable indication of the damage that it has on the financial institutions that are critical to economic growth which is very humongous. It can leads societal issues such as increased inflation, reduced economic growth and decreased foreign investment. It can also encourage an increase in crime and corruption which can slow down a country's economic

[256] Michael Marchant, Mamello Mosiana, Paul Holden and Hennie van Vuuren (2020), *The Enablers: The Bankers, Accountants and Lawyers who cashed in on State Capture*, Open Secrets and Shadow World Investigations.
[257] Lynley Donnelly, "KPMG woes deepen after VBS bank scandal" (Johannesburg, 15 Apr 2018)
[258] Michael Marchant and Mamello Mosiana. (2020). *Corporations and Economic Crime Report*: The auditors. Open Secrets and Shadow World Investigations
[259] UNODC, United Nations Office on Drugs and Crime. (2012). *Money Laundering and Globalization*. Accessed 10. May 2024.

growth. Somehow it can also retard international trade and capital flows to the detriment of investor confidence and long-term economic development.[260]

The efforts to devise a global strategy to curb money laundering has never been critical as is now. Without international cooperation, money laundering becomes an uncontrollable phenomenon. As Laundering scandals continue to be revealed, investors look up to Auditing Firms to act ethical and be accountable for the supposed audit work they do for companies, since it is investors that take the biggest knock when these scandals break, losing billions of dollars in the process.

The lack of transparency and self-discipline by the big Accounting Firms is currently posing a risk to the world economy such that it could lead to a global economic cataclysm that will result in a global stampede of governments desperately seeking a way out on one side and investors on the other trying to save their investments. Like never before, has a need arisen for Global Regulators to demand and enforce transparency and integrity in financial audit reporting. The fact that Audit Firms audit large multinational companies, yet on one side they are assumed to self-regulate themselves, with little insurance and insufficient capital, could easily trigger global financial crises. Which is why some countries like the UK and the US are calling to break up the big Accounting Firms.

7.3 TAX BASE EROSION EFFECTS:

Global expanse of business operations through global value chains, capital flows, and direct investment has identified loopholes in tax rules and friction between countries over tax revenues, tax compliance, tax sovereignty, and tax fairness.[261] Case studies like the Lux Leaks and Mossack Fonseca tax scandals revealed in the Panama Papers, exposed the whole rogue offshore finance industry by demonstrating weaknesses in understanding global tax avoidance activities by lawmakers and politicians respectively. In tax havens these arrangements are regarded as technically legal and are perceived to be legitimate in nature. The reality is that they are entirely legal until they are made illegal by the same lawmakers.[262]

The realities are that we cannot underestimate the loss of government income that is resultant of money laundering activities. Its effects are such that governments end up misreporting revenue income because of the distortions in asset and commodity price-effects that laundering has on tax collection processes and public expenditure allocation. Its dire consequences are such that individuals and businesses end up concealing their true income and the outcome being the reduction in tax revenues. This loss of income hinders government ability to fund infrastructure projects, create necessary jobs, deliver on public services, and have an increased inflation, a reduction in economic growth and a decrease in foreign investment. In some instances the illicit proceeds turn to dwarf government budgets and can easily destabilise domestic markets, thereby, leading to corruption, bribing and a loss of control over economic policies.

The seductive appeal of tax avoidance continues to loom as the biggest risk for any country since large organizations, auditors and tax advisers can easily make large returns by selling irregular tax practices and tax efficiently structured solutions which have little impact on the company revenues. The obvious questions then, is why such practices are allowed, and how could they not be detected by auditors responsible for verifying financial statements and identifying the related risks, and whether this could be construed as collusion?

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[260] Brent L. Bartlett, *The negative effects of Money Laundering on Economic Development*, report for the Asian Development Bank Regional Technical Assistance Project No.5967 Countering Money Laundering in the Asian and Pacific Region, May 2002.

[261] Qiang, Christine Zhenwei; Liu, Yan; Steenbergen, Victor. 2021. An Investment Perspective on Global Value Chains. © Washington, DC: World Bank. http://hdl.handle.net/10986/35526 License: CC BY 3.0 IGO.

[262] Robinson *Laundrymen* 269; Hill *Money Laundering - Work of Art* 28.

The biggest challenge in the whole chain of events is that it is the same audit professionals that gets to draft and design taxation laws meant to indirectly enrich the already rich, devoid of any social responsibility whatsoever. There clearly exists some information asymmetry between the global conglomerates and the Big 4 Audit Firms such that they have gained enough inside information and clout of the trade by advising governments to write laws and offshore system's rules that are to the benefit of the same clients that they consult to. They keep these laws to their liking and easy to bypass since generating large incomes from advising their clients to evade them.

Regardless of the same laws having provisions intended to penalise companies and complicit professionals who are involved in or knowing about a crime or some illegal activity done or about to, or sell tax avoidance schemes such as offshore income generation services, assets accumulation services, and money laundering ideas. This problem of global tax avoidance generally has become a huge problem, because these arrangements are technically legitimate in nature and very legal in tax havens that they operate in until somehow they are made illegal by the haven's lawmakers.

Some of the companies use the services of audit professionals to prepare and audit their financial accounts and at the same time to handle their taxation affairs or other matters. This may lead to audit professionals being involved in criminal activities unaware. The audit firms are supposed to be a watchdog built on honour and integrity, but instead they have become so big that they now focus on making profits at any cost and it is no more about reputation. Some of the global firms like Google, Vodafone, Amazon, and many more, have also been implicated in tax avoidance schemes with the help of their auditors.

These multinational companies have bought highly complex tax structures from audit firms that they use to minimise their tax obligations to the minimal. As an example in the U.K. in 2012, Starbuck made £400m in sales. But because of aggressive tax planning, the company used tax evading tactics by paying a royalty fee to the company's headquarters situated in Amsterdam. This literary meant that, by implication it ended up paying no corporate tax in the UK because the company paid a much lower rate of taxation in the Netherlands relative to the U.K.[263]

In South Africa, the county's tax revenue is deliberately and unfairly reduced by the multinational entities (MNEs) by either inflating deductible costs of productions using transfer mispricing tactics such as management fees and interests on foreign loans, advertising fees, deflating gross income through under-selling or delaying transaction dates.

The reduction in investor money into the country results in investment rates not increasing and thus a decline in sustainable growth. Although the country has managed to recover billions in tax revenue lost through transfer mispricing in the past years, there's still some loopholes in the country's Base Erosion and Profit Sharing (BEPS) strategy, such as weak legislative controls, voluntary disclosure of information by tax payers, peoples disclosure of reportable irregularities, and lack of capacity at SARS. South Africa is estimated to be losing around R7bn per year through tax evasion crimes, which is nearly 4% of total corporate tax receipts.

Using a KPMG's South African case-study mentioned in the previous chapters. KPMG came under fire for helping the Gupta family in a tax evasion and corruption scandal by overlooking the embezzlement of R30 millions of taxpayers' money to fund their 2013 family wedding of Vega Gupta. This was purportedly done though funnelling of funds through Gupta owned shell companies in Dubai and then funnelling the funds back to South Africa through another

[263] BBC News. Starbucks pays UK corporation tax for first time since 2009. BBC (London. 23 June 2013)

Gupta's company named Linkway. As auditors of all Gupta owned companies including Linkway, KPMG failed in its duty and obligation to detect and recognise any wrongdoing in this instance and therefore did not report the irregularity. In turn these suspect irregularities were classified as business expenses in the Linkway financials thus allowing them not pay any income taxes. This being regarded as illegal since it is a misstatement aimed to evade taxes. The threat of losing the company revenue resulted in them exerting pressures on KPMG auditors, into stretching the interpretation of accepted accounting and auditing standards, thus ensuring that the auditors overlook the misstatement.

In the US, the same KPMG was recently charged by authorities for peddling offshore tax shelters in turn creating billions for their clients, knowingly misleading the Internal Revenue Service about it all. Deloitte was also accused of helping a British Bank violate sanctions against Iran, misinforming regulators about how the bank omitted information on how money-laundering controls were avoided.

The New York state regulators recently also accused the same Deloitte of been implicated in a damaging regulatory probe for helping Standard Chartered to intentionally neglect to include critical information in its financial report and for the firm to yield under pressure from bank officials to keep quiet about this and other suspect money transfers which were meant to fund terror groups and Iran's weapons programmes. Evidence shown revealed that the bank used its New York office to handle 60,000 secret transfers of about £160 billion from Iranian clients suspected of funding the Iran's nuclear weapons programme and terrorist groups like Hamas, Hezbollah, and the Palestinian Islamic Jihad. Standard Chartered strongly rejected the accusations, and Deloitte denied any wrongdoing.

The trail of email evidence revealed that Standard Chartered asked Deloitte to delete references to such transactions because it was a lot of information and the Bank felt that it was too politically sensitive. The firm agreed to the Bank's request and it drafted a watered-down version of the report as indicated in the partner's email correspondence. The verdict was that Standard Chartered had hidden more than $250 billion belonging to Iran controlled banks when Iran was under international sanctions.

Evidence led indicated that the bank had contracted Deloitte to identify suspicious money transfers routed through their branches, instead their consultant assisted the bank escape regulatory scrutiny.[264] Standard Chartered was fined $340 million whilst its auditing firm, Deloitte, got fined $10 million in penalties for misconduct, violations of law, and lack of autonomy.[265] They were also banned for a year from advising any banks chartered in New York Stock Exchange.

Developments in the UK were found to be aligned to the EU's Organisation for Economic Co-operation and Development (OECD),[266] a forum in which 38 democratic governments with market-based economies, collaborate to develop policy standards that promote sustainable economic growth. And these countries use Advanced Pricing Agreements to deter tax payers from practices of BEPS. In UK, if an auditor discovers evidence of suspect tax evasion, they have the obligation to report to relevant authorities and recommend an immediate full disclosure by the client. Should the client ignore the advice to disclose, and if such appointment includes tax matters, they must cease to handle such client's tax affairs and report the cessation to the HMRC.

[264] Ebrahimi Helia. *Op sit*
[265] Ebrahimi Helia; *Standard Chartered: Deloitte rejects US claims.* The Telegraph, USA. 07 August 2012
[266] Organization for Economic Cooperation and Development, 2011. *Convention on combating Bribery of Foreign Public Officials in International Business: Transactions and Related Documents*

In January this year (Jan 2024), a UK court of appeal unanimously rejected the misguided appeal application by Clipperton and Lloyd[267], and the court denied them any relief after a UK based accountancy firm, Premier Strategies, sold them a tax avoidance scheme called Aikido. The scheme was sold as a dividend replacement scheme using a series of complex corporate and trust transactions meant to evade tax responsibilities to the advantage of their client and in so doing, transform what would otherwise be dividends, subject to taxation into tax free dividends.

In the Europe, A review of nearly 28,000 pages of confidential documents regarding court cases, secret offshore files unearthed by the International Consortium of Investigative Journalists, and government records, revealed that the big four firms assisted companies like Pepsi, IKEA and other big corporates to embrace profit shifting strategies that allowed them to slash their tax bills by billions of dollars while maintaining little presence in countries they registered in, if not just a mailbox. This investigation revealed that 340 international companies were found to have secured secret deals from a low-tax country, Luxembourg, between the years 2002 to 2010.[268]

The main audit culprits involved were PwC that had negotiated deals for hundreds of their clients, coming up with financial loans strategies amongst sister companies. PwC was fast to deny wrong doing, claiming the report was based on “outdated” and “stolen” information, further claiming that the media did not understand how the structures involved worked. But instead documented evidence revealed that PwC engaged in aggressive tax-reduction strategies. It used Luxembourg and other tax havens countries to conduct private negotiation meetings between PwC accountants and these tax haven’s officials. The European Commission opened an in-depth investigation into the scandal in 2017 and it still continues.

The amount of revenue lost due to such tax evasion activities globally, is big enough to raise a global public concern and the impact thereof is easy to can realise. The level of taxation in a country ensures such a country to have adequate funds for future public service delivery plans and achieve sustainable economic growth. The country’s deficit has economic effects such as a growing national debt that retards a nation’s service delivery plans such as provision of jobs, healthcare, education, and subsequently diminishing employment chances. As economies develop and income rise, people’s demands increases with a need for more government services like infrastructure, education and healthcare, and public transportation (Breton, 2017).

Governments needs taxpayers to contribute to the state income for it to can offer public services through infrastructure improvements plans, social security grants, and many more strategies (Nguyen and Darsono, 2022).[269] Taxes assist in establishing national stability, country’s credibility, and economic acceptance. Taxes also satisfy delivery of basic community requirements, and boost the country’s economic growth. Tax evasion therefore affects the delivery of infrastructure development plans of that country which affects its tax policy objectives with regards to the efficiency and equity of tax benefit systems.

Any changes in tax contribution patterns can result in changes of such country’s level of economic growth and therefore it’s GDP (Pattichis, 2022; Purnomolastu, 2021). In contrast, an increase can result in surpluses between tax revenue budgeted, tax revenue collected and economic growth. The abuse of tax systems and decrease in tax revenue, through the use of mechanisms such as transfer mispricing, Base Erosion and Profit Sharing (BEPS) has a

[267] Sharon Clipperton and Steven LLoyd v The Commissioners for His Majesty's Revenue and Customs [2022] UKUT 00351 (TCC)

[268] The International Consortium of Investigative Journalists; Leaked Luxembourg files expose global companies' secret deals to avoid tax. CBC News · Posted: Nov 06, 2014

[269] Nguyen, H. T., & Darsono, S. N. A. C. (2022). The impacts of tax revenue and investment on the economic growth in Southeast Asian countries. Journal of Accounting and Investment, 23(1), 128-146. https://doi.org/10.18196/JAI.V23I1.13270

negative impact on financing of the country's development programmes. Countries with a better distribution of wealth enjoy economic growth and higher approval ratings and those suffering from corruption have low approval ratings and negative effect on their GDP growth.

The close correlation between tax revenue and economic activity is a matter to be considered at all times, rising during fast economic growth and declining during recessions. Its negative impact on economic performance correlates with low civic behaviour and retards in the deliver public services such as health or education. Whilst on the efficiency side, it generates a shift of the tax burden to those that are compliant thus distorting decisions relating to consumption of goods and labour supply. On the equity side, it undermines the social contract between the state and taxpayers (horizontal equity) and weakens the redistributive nature of the tax and benefit system (vertical equity).[270]

7.4 A COUNTRY'S REPUTATIONAL RISK:

A nation's social fabric, its ethical standards and democratic institutions can be easily weaken by criminal organizations operating within that country. Every country's good reputation is arguably one of its most valuable assets, should such reputation be compromised, it can undermine that country's public's trust in its financial systems. The subsequent results can severely impact negatively on the state and can easily have adverse influence on investors. In many instances, this gives rise to informal economies especially in developing countries in contrast to the developed world, which are defined by cash and commodity oriented transactions prone to laundering illicit funds since cash payment becomes a common method of purchasing products and most often services.

Since the affected countries are perceived mostly as being vulnerable to money laundering criminals, many face strained diplomatic and trade relationships with other countries. The resultant reputational damage attributed to their involvement in irregularities reduces possible legitimate international opportunities and sustainable economic growth of such countries. It can be very difficult for such countries to attract foreign investments meant to boost their economic development and financial stability. Investor confidence drops and reluctance to engage in business or cooperate with such jurisdictions is seen as facilitating illicit financial activities.

It should therefore be encouraged for all countries to implement appropriate penalties for aggressive taxation crimes, deny home tax privileges for any suspect illicit funds accrued through tax havens, and encourage ethical tax behaviours by way of economic incentives through discounts in the corporate tax rate or other real incentive measures.[271]

The role played by political corruption and money laundering should not be underestimated, it can bring about political instability, civil disobedience and social unrest to many nations. Furthermore, it can also cause detrimental costs and effects on political facet of the societies involved, whilst enabling political officials to hide their illicit gains and avoid accounting. Practices such as kickbacks and embezzlement are often used by launders to corrupt government officials subsequently reducing the public's trust in government institutions and undermining democratic processes. Corrupt government officials have been found to be embroiled in irregularities such as noncompliance with government procedures, lack of back up information to purchases made, payment for contracts not executed, over invoicing, double debiting, and release of funds without correct approvals.[272]

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[270] Barrios, S. *et al* (2017), "Measuring the fiscal and equity impact of tax evasion: evidence from Denmark and Estonia"; JRC Working Papers on Taxation and Structural Reforms No 05/2017, European Commission, Joint Research Centre, Seville, JRC109629.

[271] Sandi Keane, 2017. Bonfire of the big four: Auditing Firms a risk to World Economy. Michael West Media

[272] FAFT-GAFI: Annual Review of Non-Cooperative Countries and Territories 2006-2007: Eighth NCCT Review. Available at: http://www.fatfgafi.org/dataoecd/14/11/39552632.pdf

As evidence to some of these activities, a report by the South African Treasury investigation on state capture, revealed how Transnet and Eskom were allegedly looted by the Guptas. The report referred to dodgy deals concluded by former Eskom and Transnet senior officials and implicated McKinsey, the auditing Firm. The report made mention of inflated prices paid for inferior quality coal to Tegeta, a Gupta company, and kickbacks of about R5 billion paid by China South Rail (CSR) to Guptas, for facilitating a multibillion Rands Transnet tender regardless of them not qualifying, thus implicating McKinsey as Transnet advisory firm during these transactions.[273]

In return, McKinsey paid for the holiday trips of Singh, the CFO at both Transnet and Eskom, after he renewed their contract with Transnet which increased from a cost base of R25 million to R49 million. In return Singh received R16 million suspected to be kickbacks from McKinsey in one month for recommending them to Transnet with an contract adjustment cost from R38.6 billion increased to R54 billion. Singh could not explain how he had accumulated the balance of R19 million in his account. The Guptas and their friends in return made R5 billion in kickbacks on that deal.

These series of scandals alleged to involve auditing firms have proved to have more far-reaching political implications. The scandals, each demonstrating fraud, lack of ethics and transparency in their own special way, had a devastating impact on South African reputation and its international status leading to unprecedented termination of important business relationships with other countries. Markets become less transparent if without credible financial statements, and the allocation of capital get compromised and negatively impact on business and society at large.

The scandals had serious implications for the country's reputation. South Africa dropped significantly in the World Economic Forum's Competitiveness Index,[274] from 47th to 61st out of 137 countries. This was also ascribed to its drastic drop from 1st to 30th place after been ranked first for seven consecutive years in the audit and reporting standards ranking. As the country scrambled to regain its status as the world's leader in terms of corporate reporting, these enormous scandals involving fraud, corruption, and unethical behaviour continued unabated causing a trust deficit amongst the society towards the audit profession that used to be characterised by integrity.

The exposed corruption, fraud and malfeasance called into question the country's overall finance system and capital markets' stability. This called for a need to focus on nation's integrity by all stakeholders in order to recoup the integrity of brand South Africa in the eyes of the global market. The aura of integrity around the audit profession became almost non-existent. The profession lost its integrity, moral ethics, and independence, and thus the opportunity to change and meet the reasonable expectations of society became urgently eminent.

Regulators like IRBA and SAICA got their hands dirtied with numerous investigations. Government demanded realignment in redress of the anomalies since affecting the core of governance itself. Auditors and Audit Firms were investigated and fined. Professionals were stripped of their professional credentials and also fined. The Audit Firms terminated some of the professional involved, whilst some resigned out of fear of reprisals, leaving the industry with a shortage of critical skills.

[273] Nicki Gules And Sipho Masondo, "Treasury drops looting bomb" News24 (Johannesburg, 29 July 2018)
[274] World Economic Forum: The Global Competitiveness Report 2017–2018

At a global level, one of the most famous scandal of note is the 2014 'Russian Laundromat' scandal, involving criminals trying to move more than £16 billion from Russia using shell companies in the UK, New Zealand, Cyprus and other 96 countries. The scandal was first flagged by Moldovan banks suspicious of numerous transactions involving large sums of money being laundered by using 21 shell companies and fake loans.

In total, 70,000 banking transactions, 112 bank accounts and 26,746 shell company payments were used. Criminal investigations against individuals and entities involved in this scheme were launched by authorities in different countries. These investigations resulted in arrests and extradition requests for some of the people involved, freezing some of their banking accounts, seizing assets and properties of these suspect individuals. About 17 UK Banks were fined millions of pounds for their involvement by regulatory authorities. As a result tight regulatory measures were introduced to strengthen AML compliance.

The 'Russian Laundromat' scandal highlighted the scale and sophistication of money laundering operations. The challenges in detecting such criminal irregularities required advanced technological interventions. The scandal also highlighted the importance of international cooperation and regulatory oversight in addressing cross-border financial crimes.

7.5 EFFECTS ON POLITICAL STABILITY AND GOVERNANCE:

Money laundering does not only affect financial and economic mechanisms of a society, it also turns criminals into powerful actors in society allowing them to gain affluence on political process. Its infiltration, along with other financial and economic crimes, has detrimental effects and costs implications that extends into the political facet of such society, bringing about inept governance, political instability, civil and social unrest. This relates to infiltration of government offices and bribery of officials such as police, judges, and politicians by organized criminals.[275]

When individuals and organizations believe they can launder money without consequence, it erodes the legal and regulatory frameworks necessary for a healthy business environment. In most instances money launderers most of the time are used to redirect capital from prime legal investments to low quality investments that simply allow for the recycling of illicit proceeds even if it entails taking a low rate of return. Launders have no motive to generate profits and thus can easily pay high premiums on the investments that will clean their illicit proceeds and protect them from suspicion. They prefer economic and commercial ventures that do not benefit the economy of the country as investment vehicles for their illicit funds.[276]

Many developing countries like South Africa, also create opportunities like privatising state owned entities with a genuine aim of promoting economic growth, increasing efficiency and better service delivery by these entities. With the intention to also create jobs and cut cost implications meant to maintain such entities on the government purse. Instead of these initiatives improving the country's economic status, they somehow attract the attention of money launderers since they are regarded as high volume transactions that works well to clean a high volume of illicit funds.

With such transactions, launderers bid higher prices for these entities, compromising and undermining a fair and legitimate bidding process between bidders by outbidding legitimate purchasers of these state-owned enterprises. Ultimately achieving their objective of being able

[275] Van Dijk Jan. 2008; *The World of Crime, Breaking the Silence on Problems of Security, Justice, and Development across the World,* SAGE Publications.

[276] NODC, Money-Laundering Cycle. (ei pvm). The Money-Laundering Cycle. Accessed 14. 8. 2014 https://www.unodc.org/unodc/en/moneylaundering/laundrycycle.html

to clean their illicitly gained money. This in turn defeats the efforts of such countries in reforming their economies by privatizing state owned entities thus stalling economic growth.[277]

The money laundering phenomenon makes it easy for criminal elements to function and expand their criminal ventures. Launderers ensure infiltration of the political sphere by financing influential politicians, bribing government officers, so that they can enjoy political protection from prosecution, acquire political influence on the government of the day, and create room to deal with blockages to their illegal activities. The exploits involved can become a major threat to political stability and security of a country and the society at large.

Furthermore, the incapacity of the judiciary and law enforcement agencies, lack of high calibre skills in the critical professional fields like auditing, legal, policing, banking and financial intelligence agencies plays a premeditated role in the increase of these crime syndicates' ability to can increasingly manage other crimes such trafficking of drugs and human beings, fraud and corruption crimes including counterfeiting or money laundering crimes. In essence, when a government is unable to perform its functions, organised crime flourishes and benefit. The implementation of anti-money laundering (AML) measures to comply with regulations by financial institutions and businesses becomes imminent. The costs for these compliance efforts, including due diligence and monitoring, can be substantial and may impact the cost of financial services but the associated long term benefits are huge and sustainable.

In South Africa, politicians, government officials private business people, have been alleged to have been somehow linked to criminal and corrupt activities at one time or the other. As a result, a State Capture Inquiry was established in January 2018, to investigate allegations of state infiltration, corruption, and fraud to the extent to which government officials were alleged to be involved in looting of the state treasury.[278] The Commission sat from January 2018 to June 2022, presided over by the now-Chief Justice Raymond Zondo. The Commission investigated improper conduct impacting on the National Treasury and the Department of Public Enterprises. It looked into various State owned Enterprises like Eskom, Transnet, South African Airways (SAA), Denel, and the Passenger Rail Agency of South Africa (PRASA), as well as government agencies like South African Revenue Services (SARS).

The final report of the Commission pointed out that indeed state capture did take place on an extensive scale. Its recommendations were that certain implicated individuals, be further investigated and prosecuted for charges of fraud, corruption, money laundering, and contravention South African laws. It recommended that some of the affected SoEs and the Asset Forfeiture Unit should take steps to recover assets attained illegally and amounts paid to involved parties as part of irregular and unlawful contracts that were entered into. It further recommended consideration to criminally charge public officials who intentionally used their power in improper ways as a statutory offence.

Over 5,000 pages of forensic detail of the report was about how the state resources were plundered, and how the Guptas tried to influence political and economic decisions. The inquiry revealed how almost every arm of the state was looted and left bankrupt by government officials and political leaders colluding with private business people. Part of the report's conclusions left answered questions for President Ramaphosa, who was Deputy President then, as to how could he stood by and overlook SoE's being looted when enough credible evidence in the public domain revealed a need to can at least prompt an inquire on a number of serious allegations.

[277] Paul Allan Schott, *Reference Guide to Anti- Money Laundering and Combating the Financing of Terrorism*, Second Edition and Supplement on Special Recommendation IX, World Bank & IMF, 2006..

[278] Haffajee, Ferial (30 June 2021*). "PRICE OF JUSTICE: State Capture Inquiry cost almost R1bn, but it saved billions more – Judge Zondo"*. Daily Maverick. Retrieved 29 April 2022.

Blurring lines between the governing political party and the state were laid bare, with party interests prioritised over Government priorities as a result of political manipulation and influences. This exposed the blatant signs of top-level white collar crime and the culture of undue influence and impunity of top government officials and many influential people. A clear breach of national security. The test that remains is whether those who have been implicated in the report shall be criminally charged and successfully prosecuted?[279] As we write, no one had been charged yet.

Another 2022 report by the Global Initiative against Transnational Organised Crime (Gitoc),[280] also revealed how South Africa was increasingly becoming a centre of organised crime, transcending national boundaries. The report revealed the existence of organised criminal networks inside and outside the state that enable, exploit and facilitate opportunities for private gain using coercive methods. The grand-scale crimes involved had filtered through to healthcare, education and parastatals. The report made it clear that there exist a proliferation of criminality between criminals, politically connected individuals, and ordinary people in illicit and corrupt practices.

The dominance of the Big 4 Accounting Firms as a cartel unprecedented in the history of global commerce, requires a joint review of all governance and regulatory requirements of the 4 firms by a globally appointed committee of regulators. The Auditing Firms require to be listed in either the London or New York Stock Exchanges so that they can be subjected to strict listing requirements like other companies. Listing in one of the bourse would force them to disclose on price sensitive matter rules including pending lawsuits and the outcomes of such lawsuits against them.

This simply means that there is a need to establish a global regulator, powerful enough to can regulate and appropriately penalise firms for wrongdoing and ensure compliance with strict global regulatory standards. And that all the firm's partners be subject to the same moral responsibilities that applies to each and every professional consistently. That auditors and audit firms are prevented from providing both taxation and audit services at the same time in order to provide an orderly competitive market between the two services. Such measures are extremely important to a wider global society and should be seriously considered.

7.6 SOCIAL EFFECTS:

The unfortunate truth is that laundering has become transnational problem with no respect for borders, since the advent of moving money from one country to another in an attempt to hide illicit gains. With advances in technology, corruption related laundering has managed to manifest itself in many ways such as grand theft of public resources, kickbacks and petty bribes, affecting fundamental development efforts. The financial impact on society extends beyond its economic consequences, influencing various aspects of social life.

Empirical studies confirm that in many developing countries, there is always a mutual connection between politics, organized crime, corruption, poor development of law, lack of enforcement tools and limited judicial autonomy.[281] The illegally derived proceeds from these crimes tend to exploit or harm vulnerable communities perpetuating social inequality and injustice.

The initial impact is a loss to the victims, their disposable income and affordability to purchase essentials gets eroded, whilst the perpetrators gain since their wealth and income increases

[279] Maseko Nomsa; *South Africa's Zondo commission: Damning report exposes rampant corruption.* BBC News, Johannesburg. 23 June 2022

[280] Global Initiative Against Transnational Organized Crime, The Global Organized Crime Index September 2022: Report, GI-TOC, 2022.

[281] Van Dijk Jan. 2008; *The World of Crime, Breaking the Silence on Problems of Security, Justice, and Development across the World*, SAGE Publications.

thus enabling them to can purchase luxury items and assets by concealing criminally attained funds. It provides the platforms for criminal such as terrorists, drug dealers and traffickers, and corrupt public office bearers to conduct and expand their criminal activities.[282] In case where the state has failed to meet people's basic needs, criminals often use such opportunities to can exploit vulnerable people, by offering them jobs, opportunities and income through criminal syndicates.

The illicit funds that get cleaned through the financial system contribute to social inequality by perpetuating crimes that disproportionately affect marginalized groups. Supply and demand of consumptions and services get to be somehow affected, but also they are likely to increase in purchase prices especially luxury items and assets. One of the critically notable post-effect of money laundering is its negative effect on income distribution. This refers to gap between the poor and the rich in terms of income distribution and increases the tendency to commit crimes and makes illicit money attractive. This is one element that makes criminal activities look lucrative to those looking to make a quick buck or live a life of luxury.

The temptation to engage in crime seems to be the only way out of poverty thus increasing the propensity to engage in crime, be it drug trafficking, laundering or violent crimes etc. This exerts pressure on law enforcement authorities and over time, it can undermine peoples trust and confidence in their leaders and institutions, creating social instability and increasing the risk of fragility, social disillusionment, violence, and undermining of rule of law. The resultant violence in turn would create rival criminal factions fighting for power and dominance over pervasive socio-political opportunities, enforcing factional cohesion, crushing community resistance and enforcing criminal rule. The key solution could be to generate incentives that create credible deterrents that sufficiently discourage those who would be tempted.

Law enforcement and regulatory agencies are seen to be spending most of their time and resources investigating and combating money laundering. These resources could be directed towards more productive and beneficial uses, such as addressing other forms of crime or investing in public services. The result is that public institutions gets undermined and compromised, and society becomes more susceptible to various forms of exploitation, contributing to a sense of unethical conduct, injustice and disillusionment thus promoting a culture of impunity.

As rule of law and the functioning of social institutions gets weakened, criminal enterprises flourishes, empowering organized crime groups and enabling them to expand their influence. The associated criminal activities and the growing socio-economic inequality that triggers a sense of insecurity and a vulnerable society, also triggers the psychological post-effects that manifests in increased stress, anxiety, social instability and a diminished sense of well-being for individuals and communities leading to civil and political unrest.

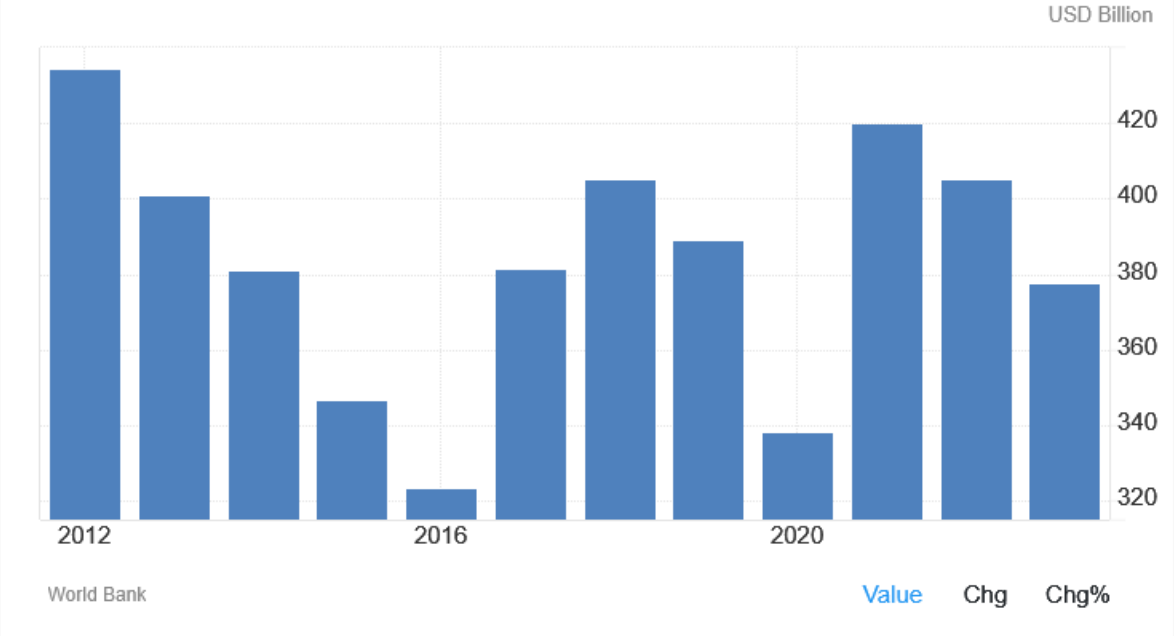
Similarly, the deficiency in government's revenue due to irregularities such as tax base erosion contributes to the plague of stripping the poor of necessary foodstuffs to eat, developmental opportunities such education and employment, affecting the country's essential infrastructure, thus perpetuating a cycle of underdevelopment that affects the entire population. Therefore the cost of public services escalates and the result is that the poor people fail to afford such services.

It is worth mentioning in this regard that South Africans are currently not that happy with the continuous public sector incompetence and increasing levels of corruption in Government. The

[282] McDowell John (Senior Policy Adviser) and Gary Novis, (Program Analyst), The Consequences of Money Laundering and Financial Crime, Bureau of International Narcotics and Law Enforcement Affairs, US Department of State, May 2001.

continuous increase in corruption incidents are perceived to be due to the incapacity of the judiciary and law enforcement agencies that should serve as deterrent to others. This has led to distrust in government institutions and resulted in sporadic protests due to the negative economic impact on the citizens.[283]

A third of South Africa's GDP which according to official data from the World Bank, was worth 377.78 billion US dollars in 2023, has been wiped out by corruption, resulting in unemployment, poor service delivery and depletion of essential social programmes.



The unemployment rate increased from an already high digit of 29% to 32.9%, the highest in a decade. South African government estimations projects that between 3 and 7 million people could be retrenched by end of 2024, the majority of those will be the poor within the society. The possibility of reversing this economic hardship soon was regrettably unlikely.

The understatement of crimes against society is such that, in many instances the victims shy away from reporting such, because of the victims displaying remarkable ineptude in involving themselves in these crimes. But the costs involved runs into millions if not billions and criminals are aware that the chances of them being reported is slim. As an examples in 2018 a bookmaker named William Hill, was fined £6.2m for breaching AML and social responsibility regulations. He is said to have gained £1.2m by allowing 10 customers to make deposits of large sums of illicitly gained funds. In another case in 2019, a partner at Child & Child named Khalid Mohammed Sharif, was given a fine of £45,000, for failing to conduct AML checks for wealthy clients believed to be linked to the Panama Papers scandal.

It can therefore be said that the economic power that accrues to criminal organizations from criminal acts such as money laundering ends up corrupting even the socio political elements of the society, and requires not only the political will, but the involvement and intervention of the society affected to be tackled as a joint effort. As the temptation of the greedy leads to the corruption of the conservative on an unprecedented scale, true accountability remains the largest of the elephants in the room for the guardians of international commerce.[284]

[283] The Democracy Development Program (DDP) by Adebimpe Ofusori; Implication of corruption on economic growth in South Africa. (October 6, 2020.)
[284] Sandi Keane, 2017. Bonfire of the big four: Auditing Firms a risk to World Economy. Michael West Media

7.7 CONCLUSION:

According to the above served information, one can conclude that, for any country to have a robust economy, there must be a reorientation of its society regarding corruption. Now that everyone knows and gets affected by the terrible effects of corruption on the economy, all nations and responsible professionals must be willing to sacrifice and do their best for the betterment and future of their respective countries regardless of the positions they occupy in society.

It should also be acknowledged that the intrinsic character of money laundering has deleterious bad effects on every country's economic growth and development. The connection between white-collared criminals, politicians, professionals, enforcing agencies and financial institutions cannot be rules out. The interdependent correlation between organized crime, money laundering activities, and high level of corruption has arguably brought about high levels of instability in the political, social and legal domains of our country. Consequently, it's the ordinary citizens that are deprived of development opportunities and economic growth. Therefore various professionals, officials and Financial Institutions are required to play a prominent role in the whole game, and without them being involved and conniving with the criminal elements, illicit operations cannot be carried out.

There is also no doubt that the global community is beginning to comprehend the extent of aggressive criminal activities such as tax evasion scandals as revealed in cases like the LuxLeaks, the disclosures around Mossack and Fonseca, and the criminal tax behaviours involved in such. That being said, it is also clear that global business activities apparently, can also be blamed for such tax avoidance schemes and their profit-sharing transactions that run across the nations, impacting on governments and other legal businesses. The obvious questions that must be asked is why these activities and the so obviously aggressive tax structures continue to be overlooked by professionals and officials like auditors and accountants responsible for verifying financial statements of firms involved in these scandal? Why do they fail to identify risks and any suspect irregularities involved for the protection of third parties?

These scandals at times involve auditor complicity and has had far reaching and adverse results for the entire profession. Because the community expects auditors to know or ought to have known or suspected that irregularities might be taking place or have already happened and need to be reported to the relevant authorities. With the current global changes, it is hoped that the auditing profession will slowly regaining the trust of business owners, management of companies, and investors at large.

It is also clear that the impact on society goes beyond economic consequences, it affects various social life liberties. The magnitude of the economic power that accrues to criminal organizations, has a corruptive effect on the socio political elements of the society.[285] The affected communities get to suffer from increased crime, environmental degradation, and other negative consequences such as affecting negatively the financial institutions that are vital to economic growth. It has limiting effect on economic productivity by deflecting resources, increasing crime and corruption opportunities. It also affects community development initiatives which then result in fewer resources available to the affected society. It involves corruption at various levels of government and private institutions and because of the large amounts of cash involved, it results in high profile scandals. Its international nature requires international enforcement regimes that require international cooperation to can successfully investigate and prosecute instigators.

[285] See http://www.scribd.com/doc/57004765/8/Dark-side-of-Money-Laundering

Chapter8: The Summary of events and related challenges.

8.1 INTRODUCTION:

The significant regulatory changes that the South Africa audit environment is undergoing since the emergence of several high level auditing and accounting scandals in past few years has resulted in drastic negative effects on the trust and the reputation that the auditing professionals had enjoyed all the past decades. Armed with their unique forensic accounting skill sets, one would assume that they are well positioned to can detect and combat irregular activities with ease. Public, and mostly investors, have always had this expectation and dependency on their professional ability to can detect suspect criminal behavior and unusual transactions which assisted them in making correct investing decisions.

But instead, public trust and confidence in the big audit firms that held so much prestige and were regarded as employers of choice by all professionals, have depleted to such an all-time low due to the role the auditors played in these major corporate failures. Of particular interest is their noticeable involvement in high-profile audit failures which experts lament to signal a decline in the auditing conduct, integrity and audit professional standards.

Considering the fact that the Big4 Auditing Firms have better resources in terms of forensic skills capacity, one would assume, they can easily pursue illicit financial flows derived from crimes such as money laundering with an intention to avoid significant audit failures. The firms have acknowledged their failures and are trying to repair their reputation and restore the trust and confidence of the commercial world that relied so heavily on their audit opinions.

The Independent Regulatory Board for Auditors (IRBA) and the South African Institute of Chartered Accountants (SAICA) have condemned audit partners and their audit firm's conduct, accusing them of collaborative wrongdoing and involvement in irregularities with multinational companies. The two South African regulators have called upon the major auditing firms to show an active interest in rebuilding the profession and the required audit credibility.

The regulators have recently followed suit by developing very strong auditing and reporting frameworks, relying on internationally accepted standards (WEF, 2012:324).[286] The framework's success is highly attributed to the effective implementation of King III code,[287] which is prescribed and recommended by South Africa's Companies Act 71 of 2008.[288]

This chapter would therefore summarise the identified corporate failures and the impact that these events have had not only on the audit profession but also the commercial world, thus impacting negatively on Government and investor confidence that the country has had all along. The chapter will also look at the envisaged future regulatory regime changes required and the Challenges faced by the industry.

8.2 SUMMARY OF EVENTS:

The role that auditors play in auditing financial records as required by law put them in a unique position to identify money laundering and other financial crimes. In chapter 2 we discussed in detail how third parties expect them to can assist in combating financial criminal behavior by detecting and reporting unusual transactions they deem suspicious with regard to good practice and applicable laws. We engaged in the concepts around Money Laundering, its

[286] World Economic Forum: The Global Competitiveness Report 2011- 2012 http://www3.weforum.org/docs/WEF_GlobalCompetitivenessReport_2012-13.pdf

[287] Jansen van Vuuren, Schilschenk, J. 2013. *Perceptions and practice of King III in South African companies*. Institute of Directors SA. http://web.up.ac.za/sitefiles/file/2013_ALCRL%20King%20III%20Study%20Report.pdf

[288] Companies Act 71 of 2008. https://cdn.ymaws.com/www.iodsa.co.za/resource/collection/CB7E5DC1-E790-4BED-9693-8AA33E0032/Companies_Act_Guide.pdf

movement and control obligations and the related control legislative regime in detail. We also discussed suspicious and unusual transactions, the Counter-measures developed to discourage related behaviors.

It is a well-known fact that each country has its own definition of money laundering, and a different process and structure to investigating and prosecute crimes related to Money Laundering. We have discussed the AML legislative regime which includes laws such as The South African Financial Intelligence Centre Act 38 of 2001 ('FICA') which imposes onerous duties on institutions such as banks to detect and report suspect irregularities, in aggregate with the Prevention of Organised Crime Act 121 of 1998 ('POCA') which criminalises crime beneficial activities. These two regulatory pieces are the backbone of the country's anti-money laundering regime. They are part of a bigger network of AML that the country introduced, some of which were amended to project a tight legislative framework meant to comply with international standards and deter any criminal behavior relating to money laundering.

Some of the laws that were amended to align with the AML strategy of the country are as follows:

- The Companies Act No.71 of 2008 (the "Companies Act"),
- Proceeds of Crime Act 76 of 1996,
- Prevention and Combating of Corrupt Activities Act 12 of 2004,
- The Protection of Constitutional Democracy against Terrorists and Related Activities Act 33 of 2004 (POCDATARA),
- The Auditing Profession Act No. 26 of 2005,
- Proceeds of Crime Act 76 of 1996.

Not taking into consideration the country's legal shortcomings on money laundering topic, in other countries such as the U.S.A, the enactment of laws such as the Sarbanes Oxley Act (2002) (SOX), serves as an excellent example to look at. Also the enactment of laws such as the Securities Exchange Act of 1934 (SEA) and the amended Private Securities Litigation Reform Act of 1995 which imposes an auditor's duty to report certain illegal acts to the Securities Exchange Commission, have made substantial impact to the AML control regimes.

The alignment of laws such as Securities Litigation Uniform Standards Act (SLUSA)[289] and the Private Securities Litigation Reform Act (PSLRA),[290] have reduced the liability exposures in Federal Securities law-cases by introducing particularized pleading requirements and proportionate liabilities to the legal processes involved. There is now evidence that shareholder litigations against auditors has also declined due to the brutal litigious environment that is becoming a deterrent in the USA.

Other efforts like the introduction of the Government Auditing Standards (GAS), the GAAS, and the International Financial Reporting Standards, introduced through regulatory structures such as the International Accounting Standards Board, the Securities Exchange Commission, and the U.S. Comptroller General, and the Public Company Accounting Oversight Board (PCAOB), has helped to reduce and discourage money laundering crimes in the U.S.

Some enactments in the UK, such as, the Companies Act 2006 as well as UK-specific legal cases, the promulgation of standards such as the Professional Standards (SAS 110), the revised suite of International Standards on Quality Management,[291] the introduction of rules

[289] The Securities Litigation Uniform Standards Act of 1998 (SLUSA), Pub. L. Tooltip Public Law (United States) 105–353 (text) (PDF), 112 Stat. 3227,

[290] Pritchard, Adam C. "The Screening Effect of the Private Securities Litigation Reform Act." S. J. Choi and K. K. Nelson, co-authors. J. Empirical Legal Stud. 6, no. 1 (2009): 35-68.

[291] International Standard on Auditing (UK) 220 (Revised July 2021) (Updated March 2023), (ISA (UK) 220), Quality Management for an Audit of Financial Statements, also becomes effective from that date.

about Liability Limitation Agreement (LLA) were regulation controls tools being utilised. The amendment of the ISA 220 (UK) Quality Management for an Audit of Financial Statements (QMAFS),[292] was based on the same QMAFS issued by the International Auditing and Assurance Standards Board (IAASB). The QMAFS plays a big role in UK's AML efforts because of its regular and effective use by regulators such as Financial Reporting Council's (FRC), Financial Conduct Authority (FCA). The Public Interest Disclosure Act 1998 (PIDA) also places the burden to report suspect activities or irregularities on all employees. These laws offer some measure of protection of auditors against civil claims such as breach of professional confidentiality and defamation.

As far as African economies are concerned, little has been done to reduce public exposure of sleaze and scandals. Global regulators including IRBA in South Africa, and UK regulators, have shown very little signs of emulating the USA in penalizing auditors specifically that assist multinationals to move money around and across borders with tax evading intentions or with lack of evidence as to the origins of such suspect money.

The South African audit regulatory structure, its mandate and competence, corresponds with the regulations in the United Kingdom, the Americas, and other progressive countries. The Auditing Profession Act No. 26 of 2005[293] governs the auditing profession, protect the public interest, and develop and maintain internationally ethical standards and measures for the profession. The Act also establishes IRBA as a regular whose main task is to act as a public protection statutory body protecting public financial interests by ensuring registered auditors and their firms deliver services of the highest quality (Van Schalkwyk 2018:2).[294]

Though Section 45 of the Auditing Profession Act 2005 (APA)[295] and the Revised Guide on Reportable Irregularities issued by the IRBA and dated May 2015.[296] It sets out a threshold and a more robust framework to regulate reportable irregularities and the investigations thereof. There still remain unforeseen idiosyncrasies about Audit Firms and the professionals that are being engaged. The trend not to report financial crimes as they happen or about to happen remains a mystery until exposed and thereafter the firms claim innocence and ignorance.

The focus by these firms is on profitability which runs throughout the auditing industry. And the citizen's reliance on them and Financial Institutions to report suspect transactions, to keep records and disclose the beneficial owners of illicit activities, becomes an impossible nightmare. It is clear that the general reliance on audit professionals to can report suspect irregularities, makes it impossible to can assist in circumventing the AML process given their sheer lack of investigative skills, the disempowered regulating authorities and the ineffective law enforcements agencies.

With evidence at hand, a reasonable man would fail to understand how the big Auditing Firms, could blindly assist the Gupta companies to suck money out of South African state owned companies, whilst they collect astronomical service fees for unprofessional services rendered (In some instances not rendered), only to wake up in the glare of the media spotlight and claim innocence. Clearly their only interest and focus has been strictly economical, intended to rake in fees whilst the public purse was being robbed.

[292] The International Standard on Quality Management (ISQM) 1, quality management for firms that perform audits or reviews of financial statements, or other assurance or related services engagements
[293] South Africa. 2005. Auditing Profession Act No. 26 of 2005:
[294] Van Schalkwyk, L. 2018. IRBA issues notice of transparency reporting for audit firms [Online]. https://www.irba.co.za (Accessed: 1 October 2018).
[295] South Africa. 2005. Auditing Profession Act No. 26 of 2005. Cape Town: Government Printer
[296] Independent Regulatory Board for Auditors, 'Revised Guide for Registered Auditors: Reportable Irregularities in terms of the Auditing Profession Act," Revised Guide, May 2015

These firms seemed to have played along instead of raising the alarm, knowingly and arrogantly undermining the country laws in their pursuit of profit. The firm's unchanged culture, displayed by the subsequent reputational scandals, has been to simply treat the regulatory penalties as another cost of doing business considering the fact that the regulatory watchdogs are incapacitated to can challenge them.

In Eskom for instance, things started to fall apart as soon as a developing auditing firm called Nkonki was bought by the Gupta family through a management buyout and forcefully introduced to Eskom. What happened next is that Eskom was exposed to excessive economic risk by paying McKinsey in 2016 about R1.6 billion "at risk" fee as a percentage profit sharing agreement they had entered into with McKinsey. The auditing firm was expected to identify savings areas in Eskom and thereafter share in the proceeds which did not happen. McKinsey had initially claimed R2.8-billion for savings that never existed nor materialised.

As if that was not enough, around 2017 Eskom signed another "at risk" consulting contract with PwC, again forcing PwC to partner with Nkonki as development subcontracting partner for a "capital scrubbing" project at astronomical hourly fee. Nkonki was still not known in the industry by then. PwC and Nkonki were also given the opportunity to work together at SAA, another State Owned Company. The trend to pair the two in tenders offered by state owned companies was a clear indication of political involvement.

As soon as PwC agreed to partner with Nkonki, the firm was rewarded with increased fees benefits and expansion of their scope to make the contract look more lucrative. In return the Firm needed to astronomically increase Nkonki's incentives. It is estimated that PwC would have made around R3.6-billion and Nkonki would have made up to R1.1-billion considering the contract adjustments that were made after, a figure disputed by PwC. The Firm also denied that it knowingly partnered with a Gupta-linked firm in order to pass some fee benefits to them. PwC ultimately received around R95-million and Nkonki received just R17.7-million from the project after public concerns about the project were raised and the contract was reviewed.

It is also evident that audit firms predatory behaviour has been more focused in wining and dining top professionals and civil servants, strategically courting politicians and other influential civilians in order to sustain their commercial existence. These alleged perceptions provided enough evidence to can confirm that between auditors, politicians, and senior officials, there was reason enough colluding and therefore enough rationale to can introduce more regulatory controls, improve legislation, increase governance and strident punitive measures.

In another case involving KPMG South Africa, the firm was accused of facilitating tax evasion for another Gupta company named Linkway Trading. They were accused of assisting the Gupta family to pay for a lavish family wedding in South Africa by laundering R30-million through Linkway. They even went further by inviting and courting the CEO of KPMG to the same wedding (Khumalo, 2017).[297] They failed to report this irregularity to the relevant authorities even though it was glaring.[298] IRBA then conducted a multi-faceted investigation into all the audit work that KPMG had done on all Gupta family-owned businesses including the work done at SARS and VBS Mutual Bank.

The last count at VBS was that the Bank had been looted about R2.7 billion by its executive directors under the watchful eye of KPMG.[299] VBS liquidators sued KPMG for more than R863-million, for the shoddy auditing work and negligence they did at the Bank, and KPMG agreed to pay R500 million as a settlement to the liquidators lawsuit. In July 2024, the former

[297] Khumalo, K. 2017. Board for Auditors Claims Evasion by KPMG. IOL: 1–7. https://www.iol.co.za/business-report/board-for-auditors-claims-evasion-by-kpmg-11476809 30 April 2018.
[298] Section 45 of the Audit Profession Act (Act 26 of 2005)
[299] Lynley Donnelly, "KPMG woes deepen after VBS bank scandal" (Johannesburg, 15 Apr 2018)

chairperson VBS Mutual Bank pleaded guilty to 33 charges and was given a 15 years jail sentence as part of a plea bargaining deal. The Audit Firm also offered to refund SARS about R23 million for poor audit services rendered and declared to donate R40 million to the charity of their choice.

Because of the political influence that the Gupta family had on government officials, their ability to influence appointment of ministers, the appointment and removal of SoE Directors, and the awarding of government tenders, had a very negative impact to some of these State owned Entities in that they incurred increased indirect operational costs (Skiti, 2017:1-2).

It has been the intentions of this thesis to focus on the significance and relevance of professional and ethical conduct of these auditors to their clients, their behavioural impact on ethical auditing, their auditing trends, the fraudulent transactions involved, their negligence and dishonest practices that kept implicating their profession and Auditing Firms that employ them in these high level scandals.

These scandals, including many others mentioned in Chapter 4, have certainly brought up some important discussions around auditor responsibilities. But the most important question that one should ask himself is whether auditors should be shouldering the blame for failing to uncover and report fraud? The exposure of these scandals, and the public outcry and backlash called for the auditing profession and Audit Firms to be investigated due to being accused of fraud, theft, corruption and being involved in money laundering exercises. Numerous serious accusations such as the ones mentioned here below were thrown at them as examples:

8.2.1 Failure to comply with accounting standards:

In the case of African Bank, it was found that the Bank failed to comply with accounting standard IAS 39, which deals with the recognition and measurement of financial instruments when it comes to the impairment of loans, as a result of this, the Bank became insolvent and was placed under curatorship and subsequently closed.[300]Deloitte was implicated in producing the Bank's fraudulent auditing reports, and it was argued that Deloitte as the bank's auditing firm, knowingly allowed these noncompliance activities and looked the other side.

8.2.2 Falsifying records:

Deloitte was also implicated in other corporate failures reported about Steinhoff and LeisureNet companies for falsifying records. In the shocking financial collapse of Steinhoff, management was accused of financial misstatements, hiding loses and inflating earnings under the auditship of Deloitte. In December 2017 the company's share price collapsed after the revelation of these accounting irregularities and breaches committed in its balance sheet. By implication, this misrepresentation of results vastly inflated the company's income, giving a false reassurance to its investors. Deloitte overlooked these accounting irregularities and did not report them as is expected by Section 45(1) of the APA. The investigations on this matter revealed that there was complicity in wrongdoing between the auditors and Steinhoff's directors. Deloitte ended up being sued by the company investors for losses they suffered when the retailer's share price plummeted.

In another case, an affidavit was filed in the North Gauteng High Court, whereby the National Prosecuting Authority accused McKinsey for colluding with Trillian and Eskom in stealing R1.6bn from Eskom. Investigations revealed that McKinsey falsified records and fraudulently invoiced Eskom for no services rendered with the help of internal Eskom officials. Om the look of things, it is alleged the payment was just for falsifying the financial statements.

[300] Justin Brown, "Deloitte partners charged" Fin 24 (Johannesburg 25 March 2018) https://www.fin24.com/Companies/Retail/deloitte-partners-charged-20180323

8.2.3 Misstatements of financials and hiding illicit funds:

In one particular case, KPMG as auditors for a Gupta' company, Oakbay Investments, was alleged to have looked away when it received half a billion rand of illicit funds from a foreign country. There was enough evidence for KPMG to can detect and deduce that something was wrong, yet it did not qualify its audit opinions on Oakbay Investments. Evidence was clear that Oakbay, a Gupta company was used to bring illicit money into South Africa using offshore shell companies based in Dubai and owned by the Gupta family. KPMG was paid millions for their service and not reporting the anomalies.

8.2.4 Concealing information/Conflict of interest:

The VBS scandal was one real classic case of corporate governance failure. Sipho Malaba, a member of the VBS audit team and a KPMG engagement partner, received a bribe worth R34m in "no repayments" loans arrangement by VBS to Betanologix, a company owned by his wife and others, and he never declared this conflict of interest. Investigations also revealed that Malaba knew that VBS was R1 billion in the red, but signed off the Bank's financials as a true reflection and pocketed a R34 million bribe. The disgraced KPMG firm agreed to pay R500 million in a lawsuit settlement by the Bank's liquidators, and Malaba faced criminal charges. Whilst the former chairperson of the Bank pleaded guilty to 33 charges and was sentenced to an effective 15 years imprisonment as part of a plea bargaining deal in July 2024.

8.2.5 Inflated revenues, cost savings & assets:

SCOPA has been interested in the services that PwC, Nkonki and Ernst & Young offered to South African Airways. It would appear that they had captured SAA. PwC and it BBBEE partner, Nkonki, were accused of very serious audit failures since they jointly took over auditing at SAA from Deloitte in 2012 till 2017 when the airline was in a crisis mode. During this tenure, the auditors signed off SAA's financial statements without qualification or concern for all those years they were contracted to audit SAA. They did not report the glaring internal control deficiencies that existed in SAA, nor did they raise alarm about the SAA's dodgy financial statements.

At that time records shows that the State had bailed out SAA with more than R50-billion since 2008, and yet no return on investment had been realised. During investigations on SAA, it was revealed that a lot of irregularities such as inflated service pricing, fronting, conflicts of interest by staff, introduction of fictitious vendors with fictitious bank accounts, fictitious work orders, overpayments, service non-deliveries and non-performance, happened with literary no value for money in return. SAA went bankrupt when government refused to bail it out, and was placed under administration and subsequently nearly closed down at the expense of 80% of its employees who got retrenched and a massive termination of SMME service contracts that were dependant on their business with SAA. This resulted in some of the businesses closing down and thus a ripple effect of more people becoming unemployed.

So the questions remain, where were the auditors as this was happening? In all these instances investigations revealed that the auditors failed in their duty to identify major misstatements and they were accused of dereliction of duty whilst they in return denied and termed it an "omission" and an "error in judgment." The investigations revealed that SAA management misrepresented in their financial reports in that they included unverified assets, non-existent inventory and unsubstantiated costs of maintenance, and that they failed to properly account for impairment of assets in their financial statements. These matters were ultimately settled by Deloitte through a "consent order".

8.2.6 Misrepresenting figures:

At Tongaat Hulett, a sugar refining company in Durban, the company executives got involved in multibillion reporting transgressions of misstatements of accounts, inflating sales profits by backdating sale agreements to the value of R2.5 billion, thus declaring incorrect profits and awarding themselves huge productivity bonuses in 2018. Deloitte had been their auditing firm

during the 6 year period that generated SA's second-biggest accounting scandal after Steinhoff. Early in 2023, the auditing firm agreed to settlement for R260m without admission of liability.

8.2.7 Auditing failures:

Whilst one auditor's failure to identify and report fraud can be devastating, it can also be an opportunity for the next one selected to clean the mess afterwards and cash in. As an example, Transnet's contracted Deloitte to investigate alleged breaches of procurement procedures that happened at its Transnet Rail Engineering and Transnet Capital Projects" under the watchfull eye of Ernst & Young. And the firm detected and reported the alleged irregularities in terms of Section 45(1) of the APA. Ernst & Young as the auditing firm that was involved then was accused of auditing failures by ignoring serious governance-flouting findings observed at Transnet in the amount of R18-million.

The scale of misrepresentation of figures and escalation of such figures should have raised the ire of Ernest & young auditors. It still baffles many as to how could the Audit Firm not report these RIs and instead turned a blind eye and covered their tracks and instead the firm changed their lead auditor who was responsible for detecting the anomalies and raised a concern about them.

8.2.8 False financial statements:

VBS is a classic case on this issue, KPMG as the Bank's auditor, under management undue influence, knowingly clamped down and falsified the Bank's audited financial statements by hiding the fact that VBS had embezzled all of the cash it claimed to have, and subsequently approved the alleged fraudulent statements whilst their auditing partner pocketed a bribe of about R34-million as previously indicated.

In the Leisurenet case it was established that the group changed its accounting policy, that the auditors played a role in financial misstatements of the groups reports by falsifying a note in the company's annual financial statements. Leisurenet's BBBEE partner named Sekunjalo, subsequently launched an unprecedented R200m law suit for damages against Deloitte & Touche over the losses suffered due to the collapsed of Leisurenet.

8.2.9 Payment of bribes and kickbacks:

McKinsey fired some of its employees after launching internal investigations to probe their deals with Gupta-linked companies and payments of kickbacks for helping SAP win State tender contracts. In another case of bribes and kickbacks, a South African Treasury investigation report[301] revealed a collusive shenanigan at Transnet in that after Nedbank Capital contract was terminated over a conflict of interest, Regiments Capital (a Gupta company) and McKinsey became partners and took over. This made McKinsey's contract value to escalate from R35.2 million to R267 million through unjustified scope extensions. And the contract was later ceded to Trillian, another Gupta company. In total, McKinsey was paid about R3.1 billion by Transnet for their involvement in the Trillian and Regiments partnership contracts.[302]

Regardless of all these audit mishaps, the expectation and trust that civil society places on auditors as protectors of societal interests emphasises the expectation that they are expected to act independent of the companies they audit at all times. It is therefore expected of them not to risk their reputational capital, built over the years, to be the subject of never-ending claims of indecorum. At the epicentre of the audit problems are corporate reporting ecosystems that have failed to serve public interests. All these accounting scandals have come about since the

[301] Nicki Gules And Sipho Masondo, "Treasury drops looting bomb" *News24* (Johannesburg, 29 July 2018) https://www.news24.com/SouthAfrica/News/treasury-drops-looting-bomb-20180729-4

[302] Nicki Gules *op sit*

enactment of the Auditing Profession Act 26 of 2005 and they are a potent abomination to the auditing profession indicative of the failure to deliver credible audit results because of lack audit independence and professional scepticism. Therefore making stronger the arguments for reinforcement of the legislative regime in the country.

With these scandals in mind, South Africa, as a member state of the FATF, has taken a stance in its AML efforts, by adopting laws such as the POCA, POCDATARA and the FIC Act etc. This is reinforced by the country's ratification stance on international legal instruments such as the United Nations Convention against Transnational Organised Crime, the International Convention for the Suppression of the Financing of Terrorism, the United Nations Convention against Corruption, and with the intensity and rate of laundering and corruption that continues to happen it remains to be said that this might not be enough.

In chapter 5 we discussed how FATF Recommendations define intergovernmental standards that need to be followed by countries to ensure that they identify and verify their clients. The recommendations require and emphasise risk assessment to be done, customer due diligence to be undertake and continuous monitoring of client transactions to deter and detect money laundering intentions. Being a FATF member and party to the global UN Conventions, South Africa must ensure that its Government Institutions are protected and positioned in such a way that they are able to maintain a global level regulatory framework and that all professional services offered are compliant with the laws of the country.

A comparable view with auditing scandals that rocked the USA around 2000's also revealed deep scars within American businesses and the profession in general. By then the industry was mostly a self-regulated industry governed solely by the American Institute of Certified Public Accountants' (AICPA) auditing standards. Because of the emergence of high level scandals such as Enron and WorldCom scandals that took place then, the need for change within the industry became indisputable for the US Government.

Because of the profession is self-regulated, there is an existing deep intertwining relationship between the auditing firms and their clients. This closeness is attributed to continuous years of monopolistic auditing service that the firms give to their clients. This was found to be the main cause of the downfall of Arthur Andersen as part of the then Big 5 Auditing firms and led to the global adoption of the MAFR by some countries.

With the Enron scandal, a lot of employees lost thousands of their jobs and their retirement investment funds. Enron shareholders also made a loss of $74 billion. Enron being one of biggest America companies, which ranked No.5 on the Fortune 500 listing subsequently filed for bankruptcy in 2001, citing a third quarter loss of $618 million and a $1.2 billion reduction in owner's equity. Investigations revealed that the company had overstated its profits by $586 million over the past 5 years under the watchful eye of Arthur Andersen as their auditing firm since 1986. This change in profitability prompted investigations by the SEC and it found that Enron's main issue was weak internal controls and aggressive accounting practices which enabled perpetration of fraud by Enron executives.

Such long standing auditor/client relationships made Arthur Andersen to be too reliant on revenue made from servicing Enron as a client, to such an extent that the auditing firm could not survive without Enron business thus collapsed. Which is one of the reason why the Audit Firm overlooked so many irregularities at Enron, allowing the company to commit fraudulent irregularities. Arthur Andersen auditors were aware of Enron's collapsing auditing standards and policies and never made any attempts to correct the situation. The firm was aware of the large-scale fraud that was happening, and that the company possessed a large amount of risk and was about to collapse at any time. But decided to overlook the irregularities and not report them. The Audit Firm started shredding their documents after the fraud at Enron was exposed

in an attempt to hide information, with the knowledge that the firm was about to be investigated. This was one of the main cause for the firm went under.[303]

After Enron, came WorldCom, a large telecommunications company based in Mississippi. WorldCom was accused of continuously decreasing its reserve accounts that were meant to cover the liabilities of its acquired companies, resulting in increases of its revenues by $2.8 billion. Seeing that this was not helping, the company misclassified its operating expenses with about $3.85 billion as long-term investments. In 2002 the company's internal auditors began to investigate the past four years of accounting practices that were engaged, only to discover a litany of suspect irregular entries. The internal auditors were told not to reveal this info to external auditors, an indication that serious fraud was happening, disregarding the client's unwarranted pressures, the internal auditors instead decided to report the irregularities to the authorities. This extensive auditing oversight was another reason that led to Arthur Anderson's downfall. After the furore, the company was forced to close shop. The WorldCom scandal cost 300,000 jobs and investors lost $180 million.

The issues uncovered by these scandals regarding both the auditing fraternity and corporate business raised the need for a prompt change in regulatory and legal regimes, and that change needed to happen fast. That is the reason why the US Congress passed laws such as the Sarbanes-Oxley Act of 2002. [304] The intention was to regulate and govern all American Stock Exchange registered companies, to increase corporate responsibility and transparency, and protect investor interests. The impact of these scandals on Government, Society, the Profession and the business was too huge to can quantify. The world started to recognize ML as one of the world's greatest social cancer. The need for whistle-blowing and in return the protection for auditors that decide to report needed to form part of AML laws, these two issues has became the centre of global debates of the day since then.

In South Africa, the need for whistle-blowing duties for auditors enshrined in section 45 of the Auditing Profession Act No. 26 (2005) (APA)[305] became a matter to be seriously considered and enforced, with the aim of generally improving audit quality. It is clear that despite the mandates of recognising whistle-blowing acts that the APA (2005) ensured, a theoretical flaw emerged with the Act not offering legal protection for auditors who, *bona fide*, complies with the Act. Unlike in the UK and the USA where auditors are already offered some means of protection proportionate to the extent of their whistle-blowing duty. Countries like South Africa still need to benchmark themselves against such efforts and identify areas where changes in law or operational aspects exists and need to be closed. Attention still need to be paid on aspects such as increasing enforcement powers of regulators, expanding access to government information, and frequently updating their Anti-Money Laundering regulations and strategies.

In many instances, auditing firms and their audit partners are not protected by law makers from delictual liabilities in case they wrongfully report a client of any reportable irregularity. The efficiency of law enforcement in many countries has not improved to such an extent that auditors feel confident in reporting suspect acts of crime. The lack of monetary rewards for auditing firms that successfully report financial irregularities is another discouraging fact. Audit Professional bodies are also expected to play a role in educating their member firms about mandatory reporting guidelines they should comply with. However, until such awareness of standards is enforced, it seems unlikely that auditing firms and their employees will embrace the idea of reporting money laundering.

[303]ABC News, Arthur Andersen Goes Out of Business. ABC News (London,December 8, 2009)
[304] Sarbanes Oxley Act (2002)
[305] SOUTH AFRICA. 2005. The Auditing Profession Act 26 of 2005. Pretoria: Government Printer.

It is clear from the research discussions that as a global phenomenon, Money Laundering has become a huge difficulty to sustainable development of many countries. It has a disproportionate effect on the poor and a destructive impact on society. As a global convener to support anticorruption around the world, the World Bank has leveraged its position around the world by recognising that public affairs transparency and accountability of senior officials are fundamental to the relationship of trust between citizens and their governments, which leverages on effective delivery of public services. And that it's important and critical for nations to work together and rebuild this trust, especially in countries affected by fragility, conflict and violence.

The World Bank, in cooperation with the IMF is effective in provision of technical assistance to risk averse countries whose financial systems are most at risk. The two institutions help countries with drafting anti–money laundering laws and regulations, awareness programs and IT solutions to detect laundering. They have also raised awareness about the importance of global cooperation and information sharing that could be of assistance to all countries. The two institutions also help countries establish and strengthen financial intelligence units, and capacity building of officials intended to pursue illicit money trails that flows through the global financial systems.

Fletcher and Hermann[306] in their book titled: "The Internationalisation of Corruption", outline political challenges for AML regimes. They are of the opinion that political immunity of politicians may be a hindrance to prosecuting money launderers. Corrupt politicians are also tempted to intentionally use AML measures to freeze funds of their opponents as a political method intended to pacify and frustrate their opponents. This action can retard and hinder the efforts of law enforcement intended to gather financial evidence against the real criminal suspects. The bank's confidentiality rules also poses a challenge to the realization of these efforts, even after strict secrecy rules has been relaxed due to FATF blacklisting and increasing international pressure since September 11 terror actions.

It has also been found that auditors and other professionals are vulnerable to money launders who seek their financial and tax advices and services with intentions to either clean some illicit money, or try to avoid paying tax by all means. These financially desperate professionals have also been found to can assist criminals with consultation services that facilitates their access to financial institutions with laundering intentions, helping them with transactions such selling or purchasing stocks, cash deposits or withdrawals, issuing or cashing cheques, sending or receiving international funds and other ways of cleaning illicit money.

8.3 THE FUTURE REGULATORY APPROACH:

The audit regulatory environment in South Africa has undergone huge significant changes that had an effect on the audit profession, requiring new regulations to be introduced with the aim of enhancing professional accountability and the promulgation of a mandatory auditor firm rotation rule by the IRBA in 2017, making huge changes to the audit profession. The MAFR rule was challenged and subsequently set aside by the High Court of Appeal (SCA) in the *East Rand Member District of Accountants v Independent Regulatory Board for Auditors* case in 2023. The court's finding was that the promulgation was beyond the legal power or authority of the act (ultra vires) and "falls to be set aside." It therefore became no longer mandatory to comply with MAFR since the ruling until further developments.[307]

The aim of some of these recent changes were to bolster efforts to hold auditors to account and enhance their independence, stimulate innovation and improve audit quality, and enhance

[306] Clare Fletcher and Daniela Herrmann, *The Internationalisation of Corruption* (, 2012) at 177-179.
[307] East Rand Member District of Chartered Accountants v Independent Regulatory Board for Auditors (113/2022) [2023] ZASCA 81 (31 May 2023)

the effectiveness of auditing and the integrity of audit regulators. These changes had presented challenges of their own, such as transitioning cost to the new changes, acquisition of new critical expertise by the firms and the understanding of the client's business every rotation time.

The audit industry continued being subjected to significant scrutiny as auditors were found to be vulnerable to money launders and had been seen to be prone to being easily swayed from complying with stipulated professional standards. The audit industry's dominance as a cartel and their being historically involved and implicated in domestic and international corporate wrongdoing also became an issue that prompted a long over-due need for a globally driven joint review of regulatory requirements. The trust around the auditing integrity and reliability was being seriously eroded in the meantime by these scandals because they involved distinguished multinational companies that had a profound global impact.

As pressure mounted towards the reluctance of regulators like the IRBA to act harshly against the firms after it had lost the MAFR case at the High Court of Appeal (SCA). The regulator made amendments in regard to the Auditing Profession Act (APA 2005) regarding the registration of auditors, prescribing the minimum qualifications for incumbent auditors, their competency standards and requirements, the validity periods for registration, and lastly the minimum requirements of registration.[308] These amendments were meant to restore public trust and confidence in the profession. In May 2024 the IRBA introduced a no-fee ADP and curb fee increase for trainees with the aim of underscoring its commitment to dismantling barriers and fostering an inclusive auditing ecosystem.[309]

The other intention for the APA (2005) amendment was to change the maximum fine per charge for an individual auditor from R200 000 to R5 million, and R15 million for an admission of guilt of professional misconduct per charge by an audit firm, which, when compared to other jurisdictions like UK and the USA still looks menial and arguably does not serve as enough deterrent.

The current argument is whether imposing higher fines will have any impact on audit firms found guilty of financial crimes since they can easily carry the cost without any impact to the revenue they create. Counter arguments are that, the higher the fines, the higher the audit service cost will be, and that will not achieve the objective of restoring the credibility of the audit profession. Audit firms with big financial resources will always be able to settle the penalties, the financial impact on these firms is just regarded as miniscule since it will be absorbed by future increases in service charges. Their brand may take a knock but only creative and enforceable regulatory changes will have any tangible impact on them. Smaller firms without the depth of resources, are the ones that will struggle to retain the type of client portfolio they have. The reality is that business for these big firms continues even with the potential damage that keeps on creeping on a daily basis.

So far the regulatory shifts made have restored a little bit of faith in the auditing profession's ability to perform its critical function in the economy effectively and uphold financial reporting standards. The negative implications that came with the scandals, the harsh penalties that were imposed, and the subsequent regulatory changes that were introduced made the profession unattractive to incoming graduates, considering the fears about harsh penalties imposed and prospects of being incarcerated should they be linked to any corporate scandals.

[308] Auditing Profession Act no 26 of 2005, as Amended: registration of registered auditors and registered candidate auditors.
[309] IRBA 2024. IRBA Announces Measures to Enhance Pipeline of Registered Candidate Auditors and Boost Profession's Appeal. (Johannesburg, May 23, 2024)

This, and the exodus of some of the professionals looking for greener pastures somewhere, has led to a shortage of skilled auditors and thus a drop in the quality of audits produced.

Global regulating bodies also followed suit by introducing changes that needed to be adopted by world nations such as the introduction of the Non-Compliance with Laws and Regulations (NOCLAR) standards. These standards were adopted by SAICA and included in their Code of Professional Conduct. The NOCLAR standards are intended to address acts of omission or commission, intentional or unintentional, committed by anyone contrary to prevailing financial laws allowing disclosures by professionals to public authorities, of any irregularities without being constrained by the duty of confidentiality to any client.[310]

The global fight against Laundering and corruption gained momentum through the Organization for Economic Cooperation that was signed by 39 countries, and the adoption of the UN Global Compact's 10th Principle. The 10th Principle commits member states to avoid crimes such as bribery, extortion and corruption, instead develop policies and strategies that are meant to address these crimes.

On the 16th April 2024, Andrew Mitchell, the UK's Deputy Foreign Secretary, announced a global call to action to tackle illicit finance compelling responsible companies to be transparent and reveal ownership, controls, and beneficiaries of all high level multinational companies, ahead of World Bank Spring Meetings held in Washington D.C. To show leadership and political commitment, the country contributed £2 million to the World Bank's trust funds which is intended to tackle corruption, money laundering, and illicit finance.[311]

Whilst in 2023 the UK Government published an Economic Crime Plan 2 (ECP2) with a cost of £400 million. The intention of the plan was to increase law enforcement resources, increase the skills capacity to fight corruption by National Crime Agency (NCA), and to support other relevant government agencies in introducing beneficial ownership registries and the sharing of such information and advanced technology that could be relied on, boosting law enforcement capacity with other countries.

Other new efforts made by the UK government were the introduction of a number of amendments such as revised suite of International Standards on Quality Management[312] and the revision of the ISA 220 (UK) Quality Management for an audit of Financial Statements,[313] The two reforms have improved the UK's audit quality management process. Furthermore there were promulgation of standards such as the SAS 110[314] and the ISA 220,[315] the amendment of some regulations[316] and the introduction of Unexplained Wealth Orders (UWOs).

[310] IRBA: *"Frequently asked questions on Non-compliance with Laws and Regulations (NOCLAR) for registered auditors."* (Johannesburg, October 2017).
[311] The Foreign, Commonwealth & Development Office (FCDO). UK government will help combat global financial corruption. (Published on: 16 April 2024) LexisNexis. UK
[312] International Standard on Auditing (UK) 220 (Revised July 2021) (Updated March 2023), (ISA (UK) 220), Quality Management for an Audit of Financial Statements, also becomes effective from that date.
[313] The International Standard on Quality Management (ISQM) 1, quality management for firms that perform audits or reviews of financial statements, or other assurance or related services engagements
[314] International Standard on Auditing (UK) 220 (Revised July 2021) (Updated March 2023), (ISA (UK) 220), Quality Management for an Audit of Financial Statements, also becomes effective from that date.
[315] The International Standard on Quality Management (ISQM) 1, quality management for firms that perform audits or reviews of financial statements, or other assurance or related services engagements
[316] The Money Laundering and Terrorist Financing (Amendment) Regulations 2019 No. 1511 have been published and may be found here – http://www.legislation.gov.uk/id/uksi/2019/1511.

On January 1, 2024 the US introduced The Corporate Transparency Act (CTA)[317] that requires disclosure and transparency around beneficial ownership of US and foreign entities doing business in the US. The Act requires firms to report their beneficial owners (Beneficial ownership information-BOI) to the government through FinCEN. Noncompliance with the Act could subject Directors to a fine of up to $10,000 per day and a jail time of up to two years. [318] As far as African economies are concerned, very little is known about comparative efforts at improving AML practices (Humphrey et al, 2011).[319] But some of progressive countries are making an effort to effect some form of changes even considering to implement the MAFR.

Estimations made by the UN's Conference on Trade and Development (UNCTAD), estimates Africa's capital flight be around $90 billion per year. This is because of the ease with which criminal individuals are connected to highly placed politicians. The fact that corruption is both a political and a law enforcement phenomenon which is destructive and cannot be just easily addressed by pure technical interventions is increasing being acknowledged.[320] It has been proven that with the help of Government officials and a variety of capable service professionals, launders can transnationally move money using a variety of available methods such opening anonymous shell companies without being questioned. This drains important financial resources away from low-income countries and weakens their ability to achieve economic stability and financial independence.[321]

Underpinning these efforts requires audit professionals and firms to be strategic in their planning and have an innovative and a very proactive approach to compliance. They should also be commitment to transparency and accountability. These rapid efforts for corporate governance has also prompted companies to focus their brand protection mechanisms on anti-corruption measures as part of their efforts to protect their reputations and their shareholder's interests. Collaborating with government's law enforcing agencies, UN agencies and civil societies companies and other stakeholders have managed to realize a more transparent global economy.

Despite the increase in regulations aimed to limit fraud incidents, the unfortunate situation is that these incidents continue to increase whilst auditors still remain considered as ideal people to can address the laundering and fraud challenges. Proponents for change dictate a number of factors prompting for a demand in harsh regulatory changes. The same demands are made in regard with the auditing profession, because of certain unwarranted auditor behaviours. There has been calls for proactive actions such as the need to streamline processes and procedures, the need for accountability and efficiency, and the need for independence and competence that should be urgently considered. Once these factors get compromised, a need to relook at audit laws comes up. The question therefore is whether we require new laws considering the compromises suffered due to the increase in audit scandals that has been observed.

With this view in mind, it is clear that the crucial regulatory aspects of the auditing profession are not being addressed adequately by law makers. The root causes why some of the above mentioned aspects are not addressed by audit profession regulations stems from the culture

[317] The ''Corporate Transparency Act''. SEC. 6402. SENSE OF CONGRESS.
[318] Andrew James Lom Rachael Hashmall. "The Corporate Transparency Act is here: Are you ready?" Norton Rose Fulbright. (United States. January 2024)
[319] Humphrey, C., Kokali, S. and Samsonova, A. (2011) The politics of transnational policy making: inpursuit of auditor liability limitation in the EU, Working Paper, Manchester Accounting andFinance Group (MAFG), Manchester Business School
[320] Department for International Development - GOV.UK: Why corruption matters: understanding causes, effects and how to address them. Evidence paper on corruption, Taxell N, Rocha Menocal et al. DFID, January 2015
[321] Economic Development in Africa Report 2020: Tackling Illicit Financial Flows for Sustainable Development in Africa, available at https://unctad.org/system/files/official-document/aldcafrica2020_en.pdf

of self-regulation that still persist in the profession. Including the cordial relationship and an "information asymmetry" between a company and its auditor, and the urge to make more profit than work as gate keepers of the public. The auditors act with impunity, without any fear of serious consequences of their adverse actions. They are seen to be the law unto themselves, having total disregard for the laws and codes of good governance.

Also, the fact that almost all the members sitting as regulators are auditors bring some doubts around their independence and the regulatory processes and procedures such monitoring and discipline of auditors, this is not assisting at all and requires to change. Even regulators themselves have identified this anomaly and agree that it should be corrected.[322] The fact that the role of the regulator is to protect the interests of society requires emphasis. And the fact that there is no provision for external supervision or evaluation of the regulator, nor requirement for accountability to the community and provision for consequence management of the regulator raises the ire for new laws to be promulgated. The proposed regulations can either take a structural shape, i.e. focusing on the structure of an industry especially that of the regulator, or behavioural regulation type that focusing on the actions of an industry.

It is for these reasons and the emergence of many high level scandals that the auditing profession needs re-regulation intended to address societal needs and expectations, more specifically, to enhance the trust of society that depends on their views and help that auditors reveal detecting illicit behaviours whilst auditing their clients.

8.4 CHALLENGES:

The South Africa audit profession is navigating through a turbulent period marked by lack of accountability, efficiency and scepticism, high levels of poor audit quality, and collusion that has impacted on both the profession's credibility and its operational dynamics. Some of these trends mostly revolve around the need to separate auditing from consulting services, the high turnover rates of staff, the increase in imposed auditor penalties, the declining pass rates of incumbent auditors, the growing concerns regarding imposed punitive measures on auditors, and the lack of global co-operation. Most concerning is poor audit quality which can impact negatively on audit firm's business and can result in decreased investment, reduced economic growth and unemployment. These challenges and many others depending on country needs have had adverse impact on the profession such that an urgent need to address them is a necessity. The following risks have been the most highlighted:

8.4.1 The need to separate auditing from consulting:

The decline in professional credibility has hit most of the big firms due to the recent succession of scandals. This has led to mounting International pressures calling on the accounting firms to legally separate their consulting work from the auditing work in order to improve the standards and transparency of bookkeeping. Leading the pack for the calls is U.K. Lawmakers demanding a "break up" of Big Four Accounting Companies.[323]

Because of the huge responsibility and control that the Audit Firms interchangeably have on the majority of global company audits, a call has been made proposing a full separation of their auditing and consultancy services which is regarded as conflicting interest by many opponents. Arguments against these calls claim that a structural separation of the two would harm audit quality, and subsequently damage competitive position as a leading capital

[322] Theunissen Garth. 'Glaring gap': Auditing watchdog wants accountants independently regulated. News24. (Johannesburg19 Feb 2024)

[323] Beardsworth Thomas, and Browning Jonathan. U.K. Lawmakers Demand Break Up of Big Four Accounting Companies. Bloomberg. 2 April 2019.

market.[324] Whilst others decided to just agree with the calls and voluntarily split consultancy services from audit services. Others said a breakup would be counterproductive and result in no change at all, since all it would do is but actually reduce audit quality and distract attention from the more practical issues that are required in line with the expectations of the society.

The whole gripe about separation or not, started with PwC setting up tax shelters for their private clients as documented in the Panama Papers scandals. Public analysts cried foul, claiming the existence of conflict of interest about the coalescing of the auditing function with business consultancy and tax advisory services. They accused the Big Four of acting as quasi-regulators of global financial system, yet enjoying unregulated opacity about their own operations with no one monitoring them. Most problematic were auditing firms lobbying for tax cuts.

The firms were accused of diverting from their basic critical role of verifying financial statements of their clients, to being 'accountants of fortune' developing aggressive tax avoidance practices for multinationals and representing their client's interests. In the process creating a set of complex financial structures that can only be solved by them or alternatively required the complicity of several technical experts from around the world to can resolve.

8.4.2 High turnover rates of staff:

Clearly, the audit profession has been struggling to attract and retain seasoned auditors due to a steady reduction in the number of incumbents choosing auditing as a profession. The decline was exacerbated by recent high level scandals that had eroded trust in the industry, and the changes in the regulatory regime that were introduced with the intention to increase audit accountability, making the profession less attractive to new entrants. The extensive and often unnecessary substantive testing that highly educated auditors are subjected to these days, spending most of their time unsure about their professional progression, has led to many leaving the audit profession.

Statistics reveal that over 80% of qualified CAs are not practicing, they are entrepreneurs, tax advisers or business consultants, and 30% of those are working in the financial services industries as financial managers, whilst 32% of the chief executives of the top 194 companies on the Johannesburg Stock Exchange are CAs.[325]

The decrease in professionals poses potential challenges in terms of securing qualified auditors that are required to ensure compliance with audit standards, audit quality and presentation of accurate financial reports. This restrictive skills resource availability is posing a significant audit quality challenge globally forcing Firms to explore many ways of retaining their talent, such as considering flexible work arrangements, changes in employee benefits, reviewing work-life balance and career progression strategies. These factors were more emphasised post-covid trends that saw many people working from home and still meeting their targets, some being offered flexy jobs to work from anywhere in the world, and others emigrating overseas for better opportunities and better foreign currency based salaries in first-world countries.

However, concerns remain that the profession continues to become less appealing due to increased pressure and the regulatory scrutiny of the profession, which might result in stringent punitive measures being applied by the state. Some deserting auditors cite profession evolution fears as one of the reason they are deserting the field, whilst those that belong to the old school of doing manual work cite integration of technology and the need for new skills

[324] Beardsworth *op sit*

[325] CRAMPTON NICOLE. 26 Of The Richest People in South Africa. Entrepreneur South Africa (Johannesburg, MAR 12, 2019)

for one to be competitive as another impediment. It has become clear the 4IR has brought its own changes that require professionals to stay informed about industry trends, relevant technological advancements and regulatory regime changes, in order for one to survive in his field of practice.

8.4.3 Declining Pass Rates:

The quality of audit staff that the system can produce, their ability to join the professional ranks and deliver audit quality, their training and development, and their long term availability are core to reaching high-quality audit standards in any country. This makes pass rates of incumbent candidacy and audit output quality to be considered hand in hand. Diversity and transformation of the profession also needs to be addressed since the perception has been that the audit profession was reserved for Europeans and Indians and indigenous Africans felt being shunned.

The fluctuating pass rates of Assessment of Professional Competence (APC) examinations over the years has been a great concern for the industry. Though the 2021 results outcome showed a considerable improvement in pass rates by 57% contrary to the 2020 pass rate of 16%, the improvement was a reflection of the broad transformation change-efforts undertaken by the profession at the time. Subsequently the pass rate for the APC exam increased to 72% over the years, with a significant pass rates increases in African candidates. Such statistics are a sign of the concerted efforts made by the accounting profession in enhancing the professional competency and diversity.

8.4.4 The concerns about quality of auditing:

However auditing improvements and efforts done, audit outcomes are still compared with ongoing concerns about the audit quality practices, especially in Government institutions. There has been so much corruption, mismanagement of public funds and any other reportable irregularities, prompting calls for audit reforms. Major firms have responded by initiating various monitoring systems, integrity checks, and irregularity reporting initiatives in order to bolster audit quality requirements.

The 2022 IRBA's Public Inspections Report[326] on Audit Quality, found fundamental problems with the understanding and application of audit standards considering the fact that 80% of audit files they had inspected had audit quality issues. The inspection report also found that audit firms were grappling with higher turnover rates, which might be the contributory factor to substandard audit quality output.

The risk effect on financial reporting and compliance is such that the audit skills shortage can significantly prejudice financial reporting and compliance factors required for ensuring transparency and trustworthiness in financial statements. This noncompliance may lead to financial irregularities and misstatements that can potentially lead to decreased accuracy delays in reporting which can easily erode audit quality and investor confidence, thus affecting the integrity of the country's financial market.

Therefore, there is a huge drive to attract more interested young graduates by ensuring that the consequential fears associated with harsh penalties they might be subjected to, are eradicated, and better career prospects are being emphasised. A lot of effort is done to showcase the evolution of the audit profession, the integration of technology into the field creating new skills set required to reshape the profession to make it more attractive to new incumbents. Yet concerns remain about the high entry requirements to study accounting, high work stress and tight deadlines, the low entry-level pay, and a reduced university student pool.

[326] Independent Regulatory Board for Auditors: Public Inspections Report on Audit Quality: With a Commitment to Promote an Improvement and a Remediation of Audit Quality. 2022.

8.4.5 Regulatory Reforms and Technological Advancements:

Some regulatory changes that include the MAFR were adopted in the USA and UK with the aim of enhancing auditor independence and reducing the risks associated with long-term auditor/client relationships. The fact that MAFR were challenged and set aside by the South African courts has been a big unfortunate setback for AML efforts in the country as some of the developing countries have moved to adopt MAFR. These regulatory shifts were meant to be part of efforts to restore faith in the audit professional ability to uphold financial reporting standards and effectively perform the critical economic functions required of the profession.

The fear experienced by auditors, their lack of technological advance in the digital auditing platforms and big data analytics which has become an increasingly integral part of reshaping the auditing landscape, is a concern for many. Auditors today are expect to use the state of the art tools in order to render an efficient service to their clients with very little margin of audit mistakes. The use of the most advanced audit techniques, modern audit software, process-oriented analysis of large data files, and robotized systems to extract and handle data in different AI files has become a daily requirement in this 4IR era. These technological solutions are meant to automate routine audit tasks, fundamentally changing the audit profession structure and system processes, and thus improving the quality and efficiency of auditing practice.

8.4.6 Enhancing sanctioning powers for regulatory bodies:

There is a desperate need to restore public trust and confidence in the profession by ensuring that the amendments made in the APA Act 5 of 2021 (Amendment Act) are complied with. The amendment was meant to increase the then maximum fine of R200 000 which could previously be imposed by IRBA in case an auditor is found guilty of professional misconduct. The maximum fine was increased to R5 million per charge for an individual auditor and R15 million per charge for an audit firm. Compared to other countries like the UK and the USA, these R5 million and R15 million respective amount are menial and arguably do not represent a significant deterrent. The increases in penalty amounts are a drop in the ocean compared to what the audit firms charge clients for major audit services. These amounts need to be significantly raised higher to compare with jurisdictions such as the USA which is imposing significant fines to audit firms and their truant auditors.

Further amendments to the APA need to be made with provisions that seek to give more powers to the regulator inclusive of search and seizure powers, subpoening powers during investigations, and the simplification of the disciplinary hearing processes which will reduce the case load and time taken to resolve cases. All of these amendments should empower IRBA to can hold auditors accountable for the opinions they make. Inevitably the effect of this would be to enhance the credibility of both the IRBA and the profession.

8.4.7 The auditor's place in the compliance ecosystem:

Professor Michael Katz,[327] in one of his Daily Maverick articles analyses the allocation of responsibility for corporate failures to all the role-players in the compliance ecosystem. He highlights that the auditor is not the only role-player involved in the compliance ecosystem.
He advocates that in some instances questions should be raised about the adequacy of the laws and codes of good practice, and the necessity to ensure implementation of the principles of good governance as dictated by the King IV report.

He considers that there are other responsible patties like:

- The management, who also have the same fiduciary duties and duties of care, skill and diligence as are applicable to directors and auditors.

[327] Professor Michael Katz. "How the compliance ecosystem helps prevent corporate failure." Daily Maverick (Johannesburg, 01 Dec 2020)

- The board of directors, who by virtue of delegating to board sub-committees and senior management, are responsible in ensuring that there is always existence of sound systems and controls.
- The audit committee, seen as a statutory committee and not a board committee whose function is a vital component of the compliance ecosystem.
- The institutional investors, who should be vigilant in assessing the reputation of directors they elect and be conscientious in monitoring compliance by directors and management.[328]

His argument is that when things fall apart, attribution of the only responsibility to the auditors is incorrect, other role players in the total compliance ecosystem must also bear the blame. Though it is self-evident that the auditors have 2 significant roles in the entire ecosystem of compliance. They have the preventative role and the detection and disclosure of non-compliance role.

The Professor is also of the opinion that it is about time that in the complexity of the modern business world, the audit model, the auditor role and the legal liability and responsibility of auditors get to be redesigned.[329]

8.4.8 Weak Law Enforcement Capacity:

Having opined on the regulatory adequacy above, the focus turns towards the adequacy of law enforcement. Many auditors have complained that the inadequate expertise of law enforcement and corruption makes it impossible for authorities to can successfully prosecute major laundering cases. This situation makes it too difficult for those auditors contemplating to report criminal activities thus encouraging a high degree of auditor apathy. Without the fear of detection, apprehension and successful prosecution, compliance suffers a severe handicap and criminals feel at home to do as they wish.

Not all hope is lost, the auditing industry has had some effective detection of money laundering, with the help of recent cases of enforcement of civil and/or criminal sanctions as a deterrents and punishment to launderers. It is important that law enforcement authorities give priority to economic crimes including white collar crimes in the fight against money laundering, without interference and political pressures.

8.4.9 Poor Audit Capacity:

Inadequate training and the lack of updates on AML regulatory regime changes are seen as the main incapacitating factors in the industry. This somehow gives a wrong reflection as if there is a general lack of interest in laundering crime issues in general. There is also poor communication, poor explanation and promotion of AML strategies by the authorities which makes it hard for auditors to can actually understand as to what is expected of them.

This result in a number of failures such as the unwillingness by auditors to can challenge their client's assumptions on suspect irregular matters, a failure to apply sufficient professional skepticism to suspect transactions, and a false sense of complying comfort in internal control systems. This tendency can give rise to a 'tick-box' auditing approach instead of encouraging auditors to question and investigate substantive audit issues they deem questionable.

In South Africa because of the country's poor business values, the sheer scale of corruption is very high and companies are easy to be used in corruption with no prospects of prosecutions. The country's economy is predominantly a cash economy with inadequate background checks on foreign investors. Checking for proceeds of crime is also outside the

[328] Professor Michael Katz, *op sit*
[329] Professor Michael Katz, *op sit*

scope of audit professionals since they have limited access to confidential information, worsened by lack of incentives should they conduct investigations. Thus the reluctance by auditors to want to police noncompliance for fear of being sued by clients they report, in the advent of an unsuccessful prosecution or false accusation.

All these challenges, at first sight, appears to be relatively easy to remedy. However, one must understand that one cannot separate the audit client from the audit professional expectations to comply with rules and laws of the country. The influential pressure from clients for a clean audit opinion and a clean bill of financial health is what is important to the business. Therefore, a new model and approach of engagement with clients is required, which will be educational to the client whilst at the same time comfortable to the auditor to can report if necessary without any reservations or fear.

8.5 CONCLUSION:

In summary, regardless of significant challenges and opportunities lying ahead, the audit profession is at a crossroads and efforts to recruit more employees and attempts to professionalise the sector are crucial steps in the right direction. The decline in professional numbers, and concerns over audit quality issues highlight the need for speedy transformation and adaptation. Increased regulatory pressure, costly penalties and socially disruptive factors has resulted in high turnover of audit professionals, leaving audit firms to struggle to find replacement auditors. Firms have been left to do with fewer qualified and licenced auditors, and corporations experience unwanted changes in audit teams, leading to mistrust, perceptions of not understanding of the client's business which can result in faulty, inefficient and costly audits.

To ensure sustained professional integrity and regain community trust in the face of evolving demands and expectations, crucial steps towards rebuilding the profession need to be attended to as an urgent matter. The lack of qualified auditors has become a significant concerns for businesses in South Africa considering rapidly evolving business ideas and processes that are augmented by advanced technological systems and the ever changing regulatory environments. The challenge is to find skilled auditors and the risk of not finding professional auditors will definitely have an impact on audit quality, financial reporting and compliance with audit standards and expectations.

The subsequent inclusion of the Non-Compliance with Laws and Regulations (NOCLAR) in the SAICA Code of Professional Conduct has been a major achievement in that it addresses acts committed by employers and their employees contrary to the prevailing laws. This inclusivity has given auditors a chance to can freely report non-compliance issues to authorities without being constrained by the confidentiality agreements entered into with the clients.

The impact of globalization and the exploding economic development of international countries has led to a less attractive audit career perspective for younger generations. Large audit firms cannot handle all the demand for big audit services and thus big multinationals have resorted to the use of a multitude of small firms in different countries to resolve the problem. The disadvantage attributed to this solution is the problems with coordination and communication among the multiple participating firms.

On the contrary, the creeping advanced audit technology is reshaping the auditing industry, with digital auditing platforms and big data analytics becoming increasingly integral to the profession. These technological advances are intended to automate routine audit tasks and fundamentally change the structure of the profession and how things are used to be done. The potential outcome being an improved audit quality and efficiency of audit practices.

Chapter 9: The recommendations and Conclusion.

9.1 INTRODUCTION:

The efforts by criminal groups to “clean” illicit money has moved from being a national problem to being an international phenomenon due to the globalisation of economies and the attempts by developing countries to attract investors with cash from neighbouring countries. This in turn has drawn the attention of international institutions and researches to consider money laundering as a serious illegal activity by virtue of its impact to good governance. And a huge obligation and expectation has been placed on all professionals, mostly auditors and accountants to detect and report this crime since they are offering services to multinational companies that might be used as conduit to money laundering activities.

To achieve these expectations much more collaboration between governments needs to be done to improve inter-governmental efforts to combat the movement of illicit funds attained through criminal activities with an intention to launder and use them within legal financial systems. More suggestions and best practices need to be shared between governments, businesses, professionals like auditors, lawyers, accountants, business consultants and any other interested parties. Their recommendations and implementation of such might contribute in further strengthening corporate financial reporting practices and deter further interest in financial crimes.

Deducting from the literature review on the topic, the involvement of auditors in the emerging high level audit scandals as discussed in chapter 4, it is clear that there is a need for a change in South African regulatory and legislative regimes to ensure coherence with international AML regulations and standards. A way forward and outlined policy improvement recommendations are made by the writer based on the challenges that have been identified. This chapter is also intended to suggest the writer’s conclusive views and possible opportunities for further research.

9.2 RECOMMENDED WAY FORWARD:

The rapidly evolving business landscape, the advanced technology and changing regulatory environments require businesses to remain agile and adaptable. It is very important for businesses to stay abreast of regulatory changes and remain legally compliant at all times. It is also important for businesses to embrace Artificial intelligence and implement advanced technology-savvy solutions meant to streamline business operations. The rapidly evolving financial business requires to be augmented with digital transformation solutions meant to enhance service delivery and assist the institutions to comply with regulations, manage risk, and improve efficiency. These advanced digital platforms should be able to assist in the risk assessment and fraud detection processes by picking up suspect anomalies, trends and patterns if there are any.

The benefits of introducing technological innovations will provide early predictions of potential compliance risks, increase efficiency and accuracy, ensure predict-modelling and real-time analysis. This can help the audit industry in reducing human error, and in return increase transparency and accountability. The FATF is also actively encouraging a trend towards the use of enhanced digital KYC systems to enhance effective KYC compliance systems and procedures. The increasing digitalization will ensure more audit efficiency and robust compliance.

In an effort to restore trust in the audit profession, an opportunity has arisen to further scrutinize the legal frameworks that govern the profession prior to making all these changes. The

domination of the audit market by the big firms urgently requires dilution of audit firm's work and introduction of innovative strategies that foster a culture that empowers audit teams to proactively address auditing challenges and seize new opportunities to resolve such challenges through the use of new technologies and new laws.

The Audit Firms are currently perceived to continue enjoying a guaranteed market advantage with huge returns and limited risks. Their combined global revenue is too big and continues to prevent effective regulatory retribution. The firms are making profits without fearing serious criminal consequences of their audit mistakes and irregular consultancy advices, or even overlooking financial crimes being committed by multinational corporations under their audit supervision. In instances where they are investigated and subsequent penalties imposed, they simply treat the penalties as another cost of doing business. Therefore new approaches, new laws, new standard rules and high punitive fines need to be introduced to force them to comply with the codes of good corporate governance, and their boards should be structured such that they have a majority of non-executive directors.

Over and above the introduction of innovative work strategies, attracting and retaining top auditing talent becomes priority. This will depend on creating a conducive and engaging work environment that promotes opportunities for career advancement, a healthy work-life balance, flexible working conditions and offering competitive salaries to make audit firms more attractive to potential employees. Investing in potential employees training and development is also pivotal for enhancing their value-add and their retention. This can include provision of continuous education programs, mentorship and coaching opportunities for new graduate incumbents.

It is also important for audit professionals to stay informed about regulatory changes in their line of duty, including industry trends and best practices, and technological advancements that are crucial to their profession and intended for their successfull future navigation. This proactive approach will also enable businesses to anticipate shifts in the market, adjust their strategies accordingly, and maintain a competitive edge.

In light of the mentioned scandals and media pressures, audit firms still display attitudinal arrogance and the culture of impunity, and in many instances they are not willing to co-operate with regulatory authorities because they know that they will never be brought to book. In most instances they are also never called to account for the individual or corporate misdemeanors, instead all that happens is termination of their services with rewards in golden handshakes.

Iraj Abedian in his resent article titled, "Audit profession needs a new Dawn" summarises it all by indicating that:

> *"the audit profession needs an urgent "new dawn", with a totally different regulatory framework, new legislation, new and effective IRBA as part of which these cozy "partnership entities" are restructured to be propriety, limited entities with credible corporate governance structures, appropriate balance sheets, and – important – with total legal and financial liability for the damages that they may cause to investors and/or nations"* [330]

Globally, there is also a need for new and different regulatory frameworks for audit professionals, and for new laws to be promulgated in line with global lessons-learned on money laundering. There is clear suggestions that the accounting watchdogs have become passively dormant and everyone agrees that they needed more enforcement powers to be effective. This calls for promulgation of new harsh laws to effectively empowered regulatory

[330] Iraj Abedian, "Audit profession needs a new Dawn" *Daily Maveric* (Johannesburg,19 March 2018)

watchdogs to enforce legal and financial liabilities for damages the auditing profession may cause to investors or third parties. The empowerment and capacitation of these regulators will change the current ways in which the Audit Firms respond to these bodies as is the current situation in the US and UK contrary to South Africa.

The incapacity of regulators defines the speed with which they deal with cases of audit failures compared to developed countries. This brings about allegations that watchdogs like IRBA are incompetent and incapable of handling their workload burden and thus cannot enforce the country's laws.

Therefore it becomes an urgent matter to strengthen the monitoring and enforcement capacities of regulatory authorities and other monitoring panels of international countries. Many argue that audit industry influence and political pressure continue to shackle regulators like IRBA's ability to act effectively. The regulator need to be independent and be seen as such, and must be linked to the country's financial surveillance systems to minimise systemic failures and noncompliance issues. The reluctance by politicians and government agencies to enforce promulgated laws should also not be allowed.

PCAOB, a U.S. regulator tasked to ensure audit quality, has made allegations about the quality of audits done by global Accounting Firms which were found to have grown increasingly flawed with significant deficiencies and lack of supportive evidence to support the given audit opinion. The Agency has warned that these deficiencies undermine investors' ability to make informed decisions.

Such deficiencies have prompted the US to make new proposals such as the AS 1000 standard, which replaced a suite of older standards that address fundamental auditor responsibilities. PCAOB is also revamping non-compliance rules (NOCLAR)[331] on how auditors must look for and deal with evidence of clients who are not complying with laws and regulations, which will amend other PCAOB standards and replace standards relating to illegal acts. This will force auditors to look for issues that could have a material effect on a company's financials, which might lead to big fines or regulatory action that threatens the business.

Audit firms have maintained their position not to want to make legal judgments, and complained about the huge amount of extra work that they would have to do. Other proposed amendments will relate to aspects of designing and performing audit procedures with respect to technology, addressing concerns over reliance by auditors on company-produced information and technology tools.

The US Congress has also taken away the ability by audit industry to self-regulate and set its own standards after these trajectories as the first step, putting this duty in the hands of the Public Company Accounting Oversight Board. But critics were instead putting the blame on PCAOB, claiming that the regulator was ineffective and too weak to act as a watchdog of the audit industry two decades after it was created. They claim that penalties imposed by PCAOB were still not deterrent enough since audit quality continues to get worse, and big audit firms preferred to be fined than report their client's unexplained wealth accumulation which may compromise their relationship. Therefore this can only mean that the fines are still too small to change and deter the audit partners and their resistance to PCAOB's efforts, thus the increase in noncompliance and increased fraud attempts by perpetuators.

UK regulators, in the contrary have indicated that auditors have no obligation to probe every minor law or regulation without sufficient supportive evidence to can rouse suspicions, and that auditors can use management's own compliance programmes as a starting point. Meanwhile the Financial Reporting Council (FRC) have already dished out substantial

[331] Non-Compliance with Laws and Regulations

penalties to audit firms for lack of or insufficient supportive evidence to support a given audit opinion.

Recently, Grant Thornton was hit with a £50,000 penalty for its 2021 audit of a local authority's pension fund, which was adjusted to £40,000 for co-operating with investigators. The investigation revealed failures in the reviewed audit which included two uncorrected material errors, but with no audit evidence obtained that the value of investments was materially accurate. Grant Thornton accepted the sanction by the FRC and took appropriate remedial steps immediately after the failures were identified. There was also no evidence to show any financial gain or benefit from the failure. In the meantime, KPMG was also hit with a £1.46m fine in March 2024 for the serious failings in its audit of M&C Saatchi. One still stands to see the impact of these substantial punitive measures on the audit industry.

The latest move has been by the International Auditing and Assurance Standards Board which has proposed strengthening fraud detection standards of financial misstatements that might not be quantitative but qualitative material, depending on the fraud instigator and the reason why it was perpetrated. All these proposals are attempts for improvement at audit quality which has remained at the core of global watchdog's strategies and are critical to restoring confidence in the profession.

Other notable suggestions on new approaches based on lessons learned has been that audit professionals need to consider audits holistically, analyse and scrutinise the management's evidence and motivation properly, and approach management assertions as serious audit risks. They also need to freely engage management meaningfully in case they identity noncompliance issues and keep audit evidence safe. Developments in other countries have also taken to higher levels by introduction of initiatives like the Unexplained Wealth Order (UWO) with an intention to seize and improve recoveries of the proceeds of corruption and crime by government officials.

Further global collaboration plans being devised include fostering of strong public/private sector partnerships intended to share information to be used in targeting resources of illicit funding and corruption, and mitigate vulnerabilities. Other intentions are meant to enhance the law enforcement response through multinational capacitation of intelligence agencies and the promulgation of new laws meant to disrupt criminal activities, recover criminal proceeds, and protect the integrity of global financial systems.

Countries should also devise plans that are intended to improve the effectiveness of the supervisory regimes and consider radical options for improvements to ensure that a risk-based approach is fully embedded. Increasing the international reach of law enforcement agencies and international information sharing can promote disruption of cross border money laundering activities, prosecution of criminals, recovery of illicit proceeds, and protection of the financial systems.

9.3 CONCLUDING REMARKS:

Although the auditing sector in South Africa faces significant challenges, there is still some opportunity for innovation, specialisation, and growth. The profession is revoltingly marked by a decline in the number of professionals wanting to join auditing as a career and the stringent regulatory change effect on the profession. A unique set of obstacles presented by regulatory changes forces the auditing industry and business at large to navigate with caution. The changes highlight a period that requires significant transformation and opportunities, but it also create challenges such as auditor emigration to better countries, remote work trends, fears about required technological innovations, and a high turnover of professionals that leave the sector for better opportunities.

One cannot overstate the importance of the opportunity to attract new talent in this changing environment. With more efforts put forth for empowering programs for previously disadvantaged young incumbents, and the proactive approach to investing in ongoing professional development and organisational strategies focused on creating a healthy work-life balance, offering competitive benefits, embracing technology, is key to securing the future of auditing professions in the country.

With these opportunistic changes, the auditing profession will be assured to can be able to navigate the present complexities and come out stronger, versatile, and more essential than ever. Deloitte's 2023 Restructuring Survey[332] has revealed that there is an opportunity for the revitalisation and growth of the profession because of the increasing need for business restructuring experts which requires a dynamic shift of professional services towards adaptation and specialisation.

In the face of these dynamic shifts and the rapidly evolving world, individual professionals should be encouraged to maintain adaptability, embrace flexibility and stay abreast of industry trends. This will ensure personal fulfilment and satisfy career progression, but also strengthen the auditing profession's capacity to adapt to the current challenges and meet future business opportunities. Businesses will also be required to adapt to these changes too. Which means they would need to embrace new technological advancements, reinvigorate their operations with the help of skilled professionals, and staying abreast of regulatory changes.

Because of the allegations that audit quality has been deteriorating in recent years, and the notable mishaps and flaws that have occurred involving the audit network that includes the "Big Four" Accounting Firms. The required professional reforms have to start with the auditors and audit firms. As the sector navigates through a turbulent period, it would require the cooperation and a will from both auditors and audit firms to recover the prestige and esteem it once enjoyed. This will only take place in the presence of a real professional shift in culture by audit professionals themselves to understand that their opinions are for public interest, and thus they need to account to the public that relies on their signed audit opinions about their client's financial statements.

The institutionalized cordial and mutual relationships fostered between auditors, politicians, civil servants and senior corporate managers requires scrutiny because such relations ultimately end up in behavior deemed unethical. This behavioral conduct has been happening over a long period and has cost developing countries like South Africa billions of Rands, retarding the promised trickle-down of wealth intended to pull the poorest of the poor out of poverty.

With many legislative change attempts made in line with global standards, it is clear that a lot still remains to be done. The alleged culpability of Auditing Firms in corporate scandals have put the credibility of the country's financial systems at stake. There is a clear line of collusion between the parties involved especially in the Public Owned Entities (SOEs). Government has in turn instituted internal reviews of the various SOE consulting contracts, and the supply chain processes that were followed with these consulting tenders, to insure that no impropriety has occurred, and in case where contracts were entered into inappropriately or procurement processes were flouted redress the situation. The Government has also established various state enquiries where large scale looting has been suspected to have happened, like the State Capture Inquiry.

[332] BusinessDay News Leader. WATCH: Unpacking the annual Deloitte Africa Restructuring Survey. BusinessDay (Johannesburg. 25 April 2024)

The implementation of these various inquiries and the continued emergence of the scandalous disasters suggest that previous reforms that were implemented might be inefficient. This calls for new and different legal and regulatory frameworks, effective independent regulators with serious deterrent punitive measures for criminal acts, and steep fines to impose where firms and the professionals are found to have colluded. The regulators should also be supported with promulgation of "new progressive legislation that gives them the power to enforce total legal and financial liability for damages the profession may cause to investors or nations."[333]

This need to empower should capacitate regulators like the IRBA with knowledgeable and skilled professionals as an eminent emergency. The reason being that, with the current non-supportive laws and lack of skilled professionals, regulators like the IRBA are unlikely to discover the undisclosed underlying transactions and even if they do, they would not cope with handling the mammoth investigative work involved. Instead auditing companies would hide the extent of their culpability and agree to settle on penalties that they easily absorb as business cost.

The other unfortunately trend is that it is the same audit firms that continue to advise government departments on these same matters and receive tenders from the same governments at the expense of taxpayers. This gives credence that corruption is both a political and a law enforcement challenge which cannot be addressed by purely technical interventions.[334] The auditor's corporate and political dominance exerts a corrosive effect upon the state's capacity to can review and challenge the firm's actions. Across the globe, it is usual that one finds an Auditing Firm that have been investigated for misstatement or irregular conduct, resulting in fines paid and settlement agreements that have proven not to be deterrent for the companies implicated. In many cases, Auditing Firms that have been forced to admit their role in irregularities get to pay these fines which are just a small dent in their financial status, and they repeatedly commit the same crimes in other jurisdictions.

In reaction to these dynamics, something drastic needs to be done to improve the efficacy of the audit, the related compliance standards, internal controls and materiality across the entire spectrum of the auditing profession. Whilst auditors give no obligation to provide absolute reassurance, there is a greater expectation for them to detect substantial risks linked to fraud and corruption transactions which is not easy to can achieve without automation.

The huge disconnect between auditing process and the effective use of technology by auditors remains a concern. Auditors should refuse to do assignments that can be easily and should be automated. At this age and time Audit firms need to embrace technological developments by ensuring that their processes and procedures take full advantage of AI-generated insights. If auditors wish to remain relevant professionals, then they need to be accountable and own their responsibilities by designing audits systems that identify financial misnomers that can result in fraudulent trails, or risk losing the exclusive rights to perform financial audits.

The novelty of this research lies in focusing on the role played by the audit sector in high level scandals involving the Gupta Companies, and more specifically the role played by auditors in assisting or facilitating those irregular behaviors involved, be it knowingly or not, which to date has been ignored. To address these challenges involved, there is a need to look at new alternative responses to some of the shortcomings in order to strengthen the work of auditors.

[333] Iraj Abedian, "Audit profession needs a new Dawn" Daily Maveric (Johannesburg,19 March 2018) https://www.dailymaverick.co.za/opinionista/2018-03-19-audit-profession-needs-a-new-dawn/

[334] Department for International Development - GOV.UK: Why corruption matters: understanding causes, effects and how to address them. Evidence paper on corruption, Taxell N, Rocha Menocal et al. DFID, January 2015

The Profession needs to question its relevance and value add by responding to some of the pettiest questions:

9.3.1 Must certain audit offences be criminalised?

Self-regulation of the audit profession with no governmental interference and little representation from various interested parties is inappropriate. The biggest challenge is the blurring line between the audit structures and the audit processes which are not divorced from those to be regulated. There is also no guarantee in the process that the public interests will be considered. Neither can self-regulation be justified where the public interest is involved, unless the regulator carries out its mandate proficiently as guardian of the public interest.

Because of laundering incidents and noncompliance with auditing laws of the country that involved assisting or advising in criminal activities, a new legislative regime is required to criminalise offences committed by auditors who 'knowingly or recklessly' provide any incorrect opinion. In this instance “recklessly” should be a subjective guiding test because a risk taken must be unreasonable in the mind of the person taking it. Because Section 93(3) of the Companies Act [335] prohibits Auditors to perform any services for any company deemed to can potentially place that auditor in a position of conflict of interest.[336] It is therefore justified that commission of the above defined criminal offences be punishable by a jail term, depending on the severity of the offence, for recklessly including misleading, false or deceptive matters in an audit reports.

The US Justice Department has already made numerous efforts in prosecuting people, sending colluding auditors to prison, and fining a number of Auditing Firms for being involved or found to be colluding in financial crimes. For better global control, other countries should adopt the same pressures to ensure that white collar crimes are dealt with. Other parties that are implicated in the compliance ecosystem, like the audited entity’s management should also be subject of criminal liability using the same 'knowingly or recklessly' principle and be sentenced to jail terms. The world need examples like as it happened after the WorldCom scandal, whereby the company’s CEO was found guilty of fraud, conspiracy and misstatements and was subsequently sentenced to 25 years in prison to deter similar future behaviours.

9.3.2 Must we make white collar crimes a predicate offence for Money Laundering?

Money laundering attracts undesirable criminals from all over in the process creating concerns about security of the citizens and degrading their quality of life. The results of the crimes committed end up eroding basic individual rights by threatening rights to life and entitlements to civilian peace and security. Therefore predicate offences serve as a basis for money laundering activities and can include various crimes, such as drug trafficking, human trafficking, smuggling, tax evasion, fraud, corruption, and embezzlement.

The scope of predicate offences must extend beyond traditional criminal activities and must include crimes like cybercrime and environmental crimes because an increase in such crimes weakens the effectiveness of current regulatory and legislative regimes thus normalising criminal behaviour within a society.

[335] Companies Act 71 of 2008.
[336] APA *Op sit*

Criminals use predicate offences to raise illicit funds to be laundered with intentions to hide its criminal source. As an example, drug trafficking can generate revenue, and using money laundering steps, the illegal source of the funds becomes easily concealed, the money gets cleaned and once it is injected in the legal system, it can be used without generating any suspicions to purchase property.

There is also an inherent susceptibility of the consulting sector of the audit profession to be exploited by criminals who have criminal intentions to clean illicit funds as a predicate crime for generating illicit funds. It therefore becomes the obligation of the professionals to report such suspect activities to the legal authorities or any interested party that might suffer any loses.

9.3.3 is there lack of required degree of audit independence and scepticism?

Section 45(1) of the Auditing Profession Act 2005 (APA) does not specifically require auditors to detect or investigate fraud however, it requires the auditor to apply professional scepticism during audits with the intention to identify any irregularities if there are any, and report if such is suspected as fraud. Common law further supports this principle with the prescription of the so-called *bonus paterfamilias* or reasonable man standard that an auditor must comply with. This standard reiterates that the duty to detect fraud can only exists if under similar circumstances, a reasonably competent and cautious auditor would have detected it and *vice a versa*, placing a greater emphasis on the need for auditors to maintain a high degree of scepticism and independence.

It is without any doubt that the number of high level of scandals that were exposed were as a result of a number of failures such as the unwillingness by auditors to can challenge client assumptions on suspect matters and the judgmental issues in major audits. This resulted in failures to apply sufficient professional scepticism to suspect transactions, and a false sense of complying comfort in internal control systems, thus inducing a tick-box approach to auditing instead of auditors engaging with substantive audit issues.

The ultimate fact is that the Auditors had lacked adequate professional scepticism during the audit work. The shoddy work done by auditors in all the case studies involved were compounded by breaches of objectivity, independence, and integrity standards, highlighting a need for professional scepticism, independence and objectivity levels to be enhanced.

9.3.4 Should we change laws to effectively hold Auditing Firms accountable?

In professional context, market power can either result from monopolistic market structures that are legal in nature, or from cartel-like behaviour by professional service providers. When cartel-like behaviours emerge, legislative regulation is required to quell abuse of dominant power by those who provide professional services within the cartel.

A second potential regulatory justification arises from the presence of externalities. From an auditing perspective, the quality of auditing practises may negatively affect investors, banks, creditors of the audited company and the society in general, besides the company itself. Negative externalities appear when poor service is rendered and its poor quality affects third parties.

Current liability rules do not have sufficient deterrent effect to prevent negative externalities, therefore legislative regulation is needed to set standards *ex ante* rather than *ex post*. The

audit scandals and escalating litigation involving Auditing Firms has also resulted in increases in insurance costs, due to insured risks involved with audit firms that audit public companies.

South Africa's commitment to anti-money laundering (AML) attempts should align with FATF's recommendations 20 and 21 which expresses an obligation on member state's professionals like Auditors, to promptly report suspicious or unusual transactions and in return member state laws should protect whistle blowers that reports in good faith from criminal and civil liability.

9.3.5 Is there a need to enhance IRBA's oversight powers?

The need to strengthen audit quality reviews requires an increase in regulatory powers of IRBA and that an empowering statutory regime be created to ensure IRBA's operational independence. The regulator should be empowered to undertake its inspection and investigations activities without external interference by politicians or the big audit firms. The regulator's Disciplinary Committee should be made up of an independent panel of professionals that exclude practicing auditors. The committee must be seen to be independent in its approach, exercise rigor and an appetite to resolve matters with speed and efficiency.

All these changes would require a thorough review of the regulator's funding model and a commitment to increase its resources, its skills capacity and technological resources. With more skilled capacity and the power to be independent in its investigations, the regulator will be stabilized and able to improve in its oversight obligations, including its efforts on follow-up process of reportable irregularities thus ensure investigations and corrective actions gets expedited.

9.3.6 The importance of international cooperation mechanisms in the AML fight?

There is an increased need for cooperation between law enforcement authorities, financial institutions and accounting firms to can reduce laundering activities. A combined, multifaceted approach between multinational business and intergovernmental agencies is the only solution to can curb corruption and other financial crimes. The international legislative reforms such as financial reporting standards (IFRS) and others are becoming global accounting standards and are firmly established in some countries like the USA that has moved to reduce the differences between GAAP and IFRS. Most countries in the IFIAR, BRICS and the G7 groups have also moved to adopt MAFR, and in Africa, countries like Kenya, Nigeria, Mozambique morocco etc. have adopted the MAFR, though with reluctance from other countries.

South Africa's affiliation in international forums such as the International Forum for Independent Audit Regulators (IFIAR), the International Auditing and Assurance Standards Board (IAASB) and the International Accounting Education Standards Board (IAESB), allows the country to stay abreast of global issues affecting the audit profession since it is important for the country to frequently evaluate and assess the relevance of its AML regulations and strategies as benchmarked with those around the world. The use of universally understood accounting standards will enforce transparency, enable market competition for the use and benefit of investors in any regulatory jurisdiction, and also make it easier to tighten globally acceptable standards and their application.

9.4 POTENTIAL AREAS OF FUTURE RESEARCH:

The high rate of findings against auditing companies indicates the need for potential areas of future research with the intention to look at how we could tighten the existing regulatory frameworks to combat laundering.

Also very little research has been done in documenting the overall impact the scandals has caused and the cost to nation. A lot of documents are starting to trickle in from the inquiries

and court decisions around this issues, and that information needs to be researched, systematically captured and analysed.

The involvement of the auditing function, knowingly or not, specifically in cases where the auditor cannot be blamed after he had done everything by the book, but the offences still happened could be explored for future structuring of standard auditing procedures.

The emerging pattern of whether forensic journalism plays a more significant detection role as societal watchdogs, and the cooperation between media and whistle-blowers is another topic that is not yet fully explored thus warrant further research. Research into these topics could help specific approaches and plans for how auditing can effectively limit fraud exposure.

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