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**AUD028 Regulation vs. Professional Judgement? The Role of
Professional Judgement in the Mandatory Audit Firm Rotation
Debate**

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ABSTRACT:

The Independent Regulatory Board for Auditors (IRBA) is currently pursuing mandatory audit firm rotation (MAFR) as a solution to a perceived lack of independence of large audit firms responsible for JSE listed company audits. There is significant pushback from various stakeholder groups, especially the audit profession. One of the key arguments against audit firm rotation is an appeal to the existing legislative and regulatory framework, and its promotion of the application of professional judgement to assess auditor independence. The argument is that the judgement exercised by the audit committee and the auditor is fundamental to assessing auditor independence. Consequently, there is argued to be no need for additional regulation. The purpose of this paper is to understand the arguments being made by the audit profession regarding the role that professional judgement plays in safeguarding auditor independence. An analysis of the academic literature regarding the audit firm rotation regulation is performed. In addition, a review and analysis of official audit firm positions, as well as individual experienced audit practitioners, is performed. Individual audit practitioner positions are obtained using an open-ended interview methodology. The findings indicate that auditors are concerned that the IRBA is seeking to regulate auditor independence when allowing audit committees and auditors to exercise their professional judgement would be more effective. There is also a clear call from auditors for audit committees of JSE listed companies to improve their independence from management and increase their understanding of their responsibilities. Improving audit committee skills, experience and independence is proposed as a better alternative to promote auditor independence than mandatory audit firm rotation. Professional judgement is considered a better alternative to regulation in regard to auditor independence. Further areas for research in a South African context are provided.

Key words: Auditor independence; Audit committee; Mandatory Audit Firm Rotation; Audit quality

INTRODUCTION AND SOUTH AFRICAN CONTEXT

As of March 2017 the independence of audit firms in South Africa and the possibility of implementing Mandatory Audit Firm Rotation is being considered by the South African Parliament. The parliamentary Standing Committee of Finance invited members of the public, interested and affected parties and stakeholders to make comments on the consultation paper on mandatory audit firm rotation (commonly referred to as MAFR) published on 25 October 2016 by the South African audit regulator, the Independent Regulatory Board for Auditors (IRBA). This has followed the announcement by the Chief Executive Officer of the IRBA in August 2016 of the IRBA's plans to implement mandatory firm rotation into legislation (IRBA, 2016a; Ziady, 2016). The regulator is advocating for a change in legislation in favour of mandatory audit firm rotation as a means of improving audit quality (IRBA, 2016b). In October 2016 the IRBA published a consultation paper, requesting written response from all interested stakeholders. The consultation paper specifically, and the intentions of the regulator generally regarding MAFR, has sparked much discussion and mixed opinions.

The IRBA believes that auditor independence is critical to achieve quality financial reporting and that this independence is compromised with respect to the audits of JSE listed companies by the large audit firms in South Africa (IRBA, 2016b). The IRBA believes that the independence of the audit firm and the audit engagement partner from the audit client is a critical contributing factor to the overall quality of the audit outcome (audit quality) and that since this independence is not at the appropriate level, the regulator is pursuing a change in regulations in favour of MAFR to increase it to an appropriate level.

LITERATURE REVIEW

Auditor independence is considered important because it has an impact on the outcome quality of the audit and enhances the credibility of the financial statements in the eyes of its users. This link between auditor independence and audit and financial reporting quality is well established in the academic literature. The auditor expresses an opinion on the financial statements via the audit report and a lack of independence could impair the quality of the audit report provided to the public and stakeholders of the company. If auditors do not remain independent, they might be less likely to report irregularities or insist that financial statements be prepared to their satisfaction impairing audit quality (Carey and Simnett, 2006).

In order to assess the impact of audit independence on audit quality, a recent study by Tepalagul and Lin (2015) suggests the use of a four-dimensional approach consisting of (a) client importance, (b) non-audit services, (c) auditor tenure, and (d) client affiliation with audit firms. Figure 1 below demonstrates how the auditor's and client's incentive can create situations which may pose a threat to the independence of the auditor.

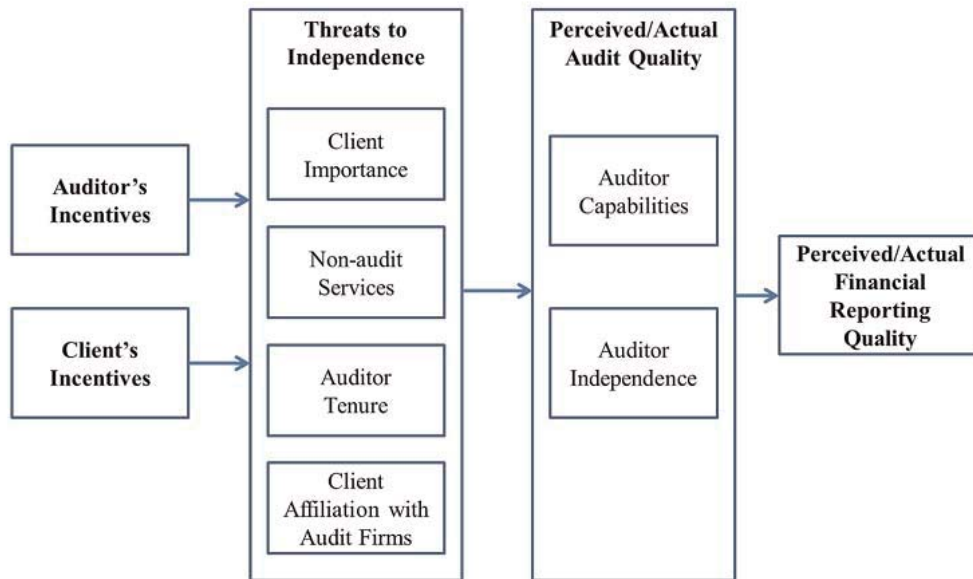


Figure 1. A framework for assessing the impact of auditor independence on audit quality.

Source: Tepalagul and Lin (2015)

As can be seen from Figure 1 above, audit quality consists of two components, namely, auditor capabilities and auditor independence. This shows the clear link between the independence of the auditor and the actual, as well as perceived, quality of the audit and financial reporting. An impaired independence of the auditor with respect to the audit client management, will consequently negatively impact the quality of the financial reporting. The threats to independence identified in Figure 1 above therefore have an adverse impact on the auditor's independence, and thus in turn negatively affects the quality of the company's financial reporting.

However, a few key questions need to be answered in the South African debate over mandatory audit firm rotation (MAFR):

1. Is auditor independence on JSE listed company audits compromised as the IRBA contends?
2. Does long auditor tenure impair auditor independence?
3. Will mandatory audit firm rotation improve auditor independence and consequently, audit quality and financial reporting quality?
4. Will regulation of auditor independence remove the need for stakeholders such as shareholders, audit committees and the auditor themselves to apply professional judgement in regard to auditor independence?

(Harber, 2016; Bam, 2017; Shango, 2017)

According to various sources (King and Natesan, 2016; Newton-King, 2016; Ramon, 2016; Bam, 2017; Bourne, 2017; Oddy, 2017; SAICA, 2017; Shango, 2017), these are some fundamentally important questions that many of the stakeholders in the South African debate are claiming need to be properly considered and researched before a decision on MAFR is made by the IRBA or the South African Parliament, who is ultimately responsible for changing legislation. This is a call to academics to perform more research in these areas.

The following is a brief literature review of the international literature.

Research regarding auditor tenure

A recent study by Tepalagul and Lin (2015) is a very important contribution to the MAFR debate. The study consisted of a comprehensive review of academic research pertaining to auditor independence and audit quality. Through a review of published articles during the period 1976-2013 in nine leading international journals related to auditing, most studies concluded that long auditor tenure does not impair independence (Tepalagul and Lin, 2015). In fact, according to Tepalagul and Lin (2015) most empirical findings are consistent with longer auditor tenure not resulting in lower financial reporting quality.

It is the intention of the IRBA to impose MAFR on a rotation period of 10 years, meaning that the audit firm will be forced to rotate off the JSE listed company after the 10th year of appointment (IRBA, 2016b). The IRBA is wanting to implement this 10 year rotation period in order to limit the tenure of the audit firm, since audit tenure is believed to be the primary reason for a growing lack of auditor independence on the JSE company audits, an opinion that has been expressed clearly in the IRBA consultation paper (IRBA, p.17, 2016b). However, if MAFR is being considered as a means to limit the tenure of audit firms, and therefore improve auditor independence, audit quality and financial reporting quality, then it is submitted that academic research is not in favour of this change in regulation being effective. As the above review of literature reveals, most studies show that long auditor tenure does not reduce auditor independence, audit quality or financial reporting quality.

Research regarding audit partner (not audit firm) rotation

Recent studies have mostly concerned themselves with audit partner (auditor) rotation (Bowlin et al., 2014; Daugherty et al., 2012; Laurion et al., 2015; Tepalagul & Lin, 2015), rather than audit firm rotation.

Again, there is some degree of mixed results in the academic literature but generally audit partner rotation has been found to improve auditor conservatism and audit quality in regimes mandating audit partner rotation (Cameran et al., 2012). Audit partner rotation has been found to improve the quality of audits and financial reporting - and South Africa already has this law in place in section 92 of the Companies Act, as is discussed further below.

Currently South Africa does not legislate the mandatory audit firm rotation (MAFR) as has been implemented in the European Union in 2014 (European Commission, 2015), but rather follows a system similar to the United States, with auditor rotation required every five years (i.e. of the individual audit partner, not the entire firm). This includes a cooling-off period of two years, as prescribed by section 92 of the Companies Act, 2008.

It is interesting to note that the IFAC Code of Ethics for Professional Accountants, the international code governing auditors and professional accountants, requires the individual audit partner, on a listed company audit engagement, to rotate every seven years, but section 92 of the South African Companies Act imposes a stricter five-year rotation period.

Research around Mandatory Audit Firm Rotation (MAFR) specifically

Unfortunately, there is very little research on the effectiveness and consequences of audit firm rotation specifically. According to Hay (2015) the rotation of audit firms is a difficult area to research because there are so few practical situations where it has been enforced. As a

result, “there is no clear evidence about whether it is effective” (Hay, 2015). According to Bédard and Compennolle, the authors of chapter 20 of the highly respected “The Routledge Companion to Auditing” (2014), as quoted by Hay (2015), “academic research has been unable to provide clear answers about the consequences of mandatory audit firm rotation”.

According to Cameran et al. (2015) there has been little research into either the benefits or costs of MAFR that could inform regulators for policy making.

However, there has been some research specifically on Mandatory Audit Firm Rotation (MAFR) in other countries. Three key studies specifically focus on MAFR and examine the effects of MAFR in countries that have adopted it. These studies are important primarily because they have been performed in countries where MAFR has been adopted and the studies have attempted to measure the impact that MAFR has had on the quality of the audit and the quality of financial reporting. This should be considered significant research on the topic and South African regulators should take note of these findings. There are many opinions on MAFR. There are many vested interests and biased parties involved in the debate. But who has objectively, using a rigorous academic methodology, actually studied the effect that MAFR has on the quality of the audit and the quality of financial reporting? Very few studies have done that.

There are various reasons for why there have been so few studies on the impact of MAFR. Firstly, there are very few countries that have implemented MAFR for periods long enough to enable researchers to measure the effects of MAFR. The European Union has only just implemented MAFR in 2014 and the impact of these regulations is yet to be seen. Secondly, the impact of MAFR is difficult to measure. How does one measure the change in quality of an audit or of financial statements? It can be done, and a small number of studies have done so.

So, although there is very little research on MAFR specifically, there are these three studies that examine the effects of MAFR in countries that have adopted it:

1. Jackson, Moldrich, and Roebuck (2008) - research conducted in an Australian context.
2. Ruiz-Barbadillo, Gómez-Aguilar, and Carrera (2009) - research conducted in a Spanish context.
3. Cameran, Francis, Marra and Pettinicchio (2015) - research conducted in an Italian context.

To summarise their findings, it can be concluded that none of these three studies are in favour of pursuing mandatory audit firm rotation. All three studies concluded that MAFR will not improve the quality of audits or financial reporting.

The purpose of this paper is to perform an exploratory study on the 4th question above.

SOUTH AFRICAN RELIANCE ON PROFESSIONAL JUDGEMENT

The auditing profession in South Africa places a large degree of reliance on the profession's ethical standards to internally assess (or self-assess) threats to its independence as auditor and put appropriate measures in place to reduce those threats to an acceptable level. If the

threat cannot be reduced to an acceptable level, the auditor should not proceed with the audit engagement.

All registered auditors in South Africa are overseen by the IRBA. The IRBA Code of Professional Conduct (CPC), a guide outlining proper conduct for auditors, identifies two components of “independence”, namely “independence of mind” and “independence of appearance”. The CPC requires the auditor to seriously consider the reality of their independence from the audit client and make decisions objectively and without undue influence (independence of mind), as well as how an informed outsider may view the auditor-client relationship (independence in appearance).

The CPC therefore identifies the types of threats which may threaten the independence of auditors and provides guidance on safeguards which may be put in place to reduce the threat to an acceptable level. The CPC also identifies situations where the threat to independence is so significant that no safeguards can be put in place, thus requiring the auditor to not proceed with the engagement.

The CPC, however, does not provide guidance on every situation in practice which may threaten the independence of auditors. As such, the CPC relies on the auditor to apply their minds and exercise professional judgement when they encounter a situation for which no specific guidance has been provided in the CPC. The CPC thus requires the auditor to exercise professional judgement to identify threats to their independence, assess the significance of the threat and then put appropriate measures in place to bring the threat down to an acceptable level where the auditor’s independence will not be compromised.

Given the public interest, in terms of ISQC 1 (the quality control standard), the audits of all listed companies are required to undergo an engagement quality control review (EQCR). The purpose of the EQCR is for the reviewer (who is an audit partner (or on an equivalent level) who is not involved in the performance of the audit) to review the judgements made by the engagement partner and challenge them where he/she feels that the engagement partner has exercised professional judgement inappropriately. The EQCR process therefore provides further assurance that the auditor has acted with independence, objectivity and professional behaviour in carrying out their duties.

In addition to the exercise of professional judgement by the auditor through professional and ethical standards, the Companies Act No 71 of 2008 (“Companies Act”) has several legislative requirements which have been put in place to promote the independence of the auditor. While these are legislative requirements, the exercise of professional judgement is integral in ensuring that the legislative requirements are complied with.

Section 90 of the Companies Act requires the auditor to be appointed annually by the shareholders at the annual general meeting. The shareholders are one of the users of the financial statements and if the auditors are not perceived to be independent by the shareholders, the shareholders can apply their minds and choose to not re-appoint the auditors. Section 90(2) also specifies individuals who may not be appointed as the auditor. Section 90(2) thus safeguards against situations which may cause the independence of the

auditor to be impaired. Shareholders therefore must be cognisant of the requirements of section 90(2) in exercising their rights to appoint the auditors.

Furthermore, in terms of section 94 of the Companies Act, all public and state owned companies are required to appoint an audit committee. Section 94 further requires the audit committee to assess the independence of the auditor prior to recommendation for appointment and must approve any non-audit service fees. The exercise of these duties requires the members of the audit committee to exercise their minds and carry out their duties in the best interest of the company, in good faith and in accordance with their fiduciary duties as mandated by section 76 of the Companies Act. This has implications that the members of the audit committee may be held liable under section 77 of the Companies Act for any loss or damaged suffered by the company because of the audit committee members failing to act in accordance with section 76. Considering these statutory requirements, the audit committee is a key gatekeeper of auditor independence as even if the auditor did not exercise professional judgement appropriately in identifying and responding appropriately to threats to their independence, the audit committee should have applied their minds as to whether the auditor was independent prior to recommending the auditors for appointment.

Although not a statutory requirement, the King IV Report on Governance for South Africa ("King IV"), through its recommendations, also encourages the audit committee members to exercise their minds in carrying out their duties. Principle 8 of King IV recommends that the audit committee manages the relationship between management and the auditor and continually assesses the appropriateness and independence of the auditor, recommending them for appointment to the shareholders. In terms of principle 1 of King IV, in performing these duties, the members of the audit committee should, exhibit the characteristic of integrity which entails acting in good faith and in the best interest of the company. This therefore implies applying their minds to determine whether their actions are in good faith and in the best interest of the company.

SUMMARY REVIEW OF OPINIONS REGARDING PROFESSIONAL JUDGEMENT

There are various professional standards, ethical considerations and legislation in place which the auditors and audit committees have to exercise their minds and apply professional judgement in order to ensure that the auditor is independent. Many argue that the professional judgement of all these parties is fundamentally critical to upholding auditor independence (Harber, 2016; Bam, 2017; Bourne, 2017; Oddy, 2017; Shango, 2017). Furthermore, they believe that audit firm rotation regulations (MAFR) will significantly reduce the role of experienced professionals, who are in a position of deep understanding of the context of the company and any actual threats to auditor independence, to apply their judgement to whether or not the auditor is independent of the company. According to this reasoning, implementing MAFR will reduce the reliance on professional judgement.

In October 2016 the IRBA published a consultation paper outlining the details of their intention to implement MAFR on a 10 year rotation basis with a 5 year cooling off period, effective in 2023. The consultation paper explicitly requested interested parties and stakeholders to provide written responses to the content in the paper. These responses to the IRBA consultation paper were provided by the deadline date of 20 January 2017.

The official responses from the following key stakeholders have been reviewed for the purpose of this summary discussion on the role of professional judgement in ensuring auditor independence:

Stakeholder: The “Big 4” Audit Firms, namely PWC Inc., Deloitte Inc., EY Inc. and KPMG Inc.

The commonly agreed and recognised distinction between the audit firms (Marx, 2009; Rapoport, 2016) has been used in this study and is as follows:

- “Big four” audit firms refer to the largest four accounting and audit firms globally, namely Deloitte Inc., PricewaterhouseCoopers Inc. (PwC), Ernst & Young Inc. (EY) and KPMG Inc.. These four firms are also referred to as “large-tier” firms (ICAEW, 2016).
- The non-big four firms are either mid-tier or small-tier firms depending on their respective global size, global presence and capabilities as an audit firm in terms of resources (ICAEW, 2016; Rapoport, 2016).

All four of these audit firms provided an official response to the IRBA. The responses were written by Dion Shango (CEO of PWC Southern Africa); Lwazi Bam (CEO of Deloitte Africa); Michael Bourne (EY South Africa Professional Practice Director); and Michael Oddy (KPMG South Africa Head of Audit).

Stakeholder: The South African Institute of Chartered Accountants (SAICA)

SAICA is a professional accountancy body in South Africa, representing chartered accountants. All the registered auditors in South Africa are chartered accountants who are members of SAICA. SAICA is an active organisation in the audit industry of South Africa.

The response from SAICA was written by Mr Terence Nombembe, the Chief Executive Officer of SAICA.

Stakeholder: The International Federation of Accountants (IFAC)

The IFAC is the global organization for the accountancy profession, comprising of over 175 members and associates in more than 130 countries (including South Africa) and jurisdictions, representing almost 3 million accountants in public practice, education, government service, industry, and commerce. The IFAC Board established the International Ethics Standards Board for Accountants (IESBA). The IESBA is the independent standard-setting body that serves the public interest by setting robust, internationally appropriate ethics standards, including auditor independence requirements, for professional accountants worldwide. The IESB compiled in the Code of Ethics for Professional Accountants which is the basis of the accountant and auditor ethics codes in South Africa.

The response from the IFAC was written by Mr Fayez Choudhury, the Chief Executive Officer of the IFAC.

Stakeholder: The CFO Forum

The CFO Forum describes itself as a high-level discussion group formed and attended by the Chief Financial Officers of major JSE listed and larger state-owned companies with broad sectoral coverage ranging from financial services, mining, retail, media, telecoms,

medical services and paper/packaging. Its aim is to contribute positively to the development of South Africa's policy and practice on financial matters that affect business on behalf of its members, who represent a significant part of South African business. The CFO Forum was created in 2011.

The response from the CFO Forum was written by Ms. KC Ramon, the Chairperson of the CFO Forum, CFO and executive director of AngloGold Ashanti Ltd., a non-executive director on the boards of MTN Group Ltd. and Lafarge (France).

Of the above stakeholder responses, nothing explicitly regarding the role of professional judgment was contained in the CFO Forum and the IFAC submissions. However, significant arguments in this regard were made by each of the “big 4” audit firms and SAICA. Here follow quotations from these stakeholder response letters submitted to the IRBA, specifically regarding the role of professional judgement in maintaining a high degree of auditor independence on JSE listed company audits, as well as the threat that MAFR poses to the reliance on this professional judgement.

From PWC Inc.

“In South Africa there are several positive measures in place that contribute to auditor independence. These include:

- a) The IRBA Code of Professional Conduct;*
- b) Audit partner rotation as set out in the Companies Act, 2008, (“Companies Act”);*
- c) Cooling-off periods for the auditor as set out in the Companies Act;*
- d) Statutory obligation of the Audit Committee in terms of the Companies Act to ensure auditor independence;*
- e) Appointment of the auditor by shareholders at the annual general meeting as set out in the Companies Act;*
- f) Disclosure of audit tenure;*
- g) Additional disclosure which has now been brought into the Report on Corporate Governance for South Africa 2016, (“King IV”);*
- h) International Standards on Auditing; and*
- i) Revisions and additions to the auditor reporting standards which have resulted in a significantly expanded auditor report including the communication of Key Audit Matters.”*

(Shango from PWC Inc., p.2, 2017)

“The Audit Committee fulfils an important role in a properly functioning capital market like South Africa in overseeing the external audit process and making the auditor appointment decision. MAFR undermines this responsibility and takes away the audit committee’s freedom to decide which accounting firm best meets the needs of the company and its shareholders. It conflicts with their statutory responsibilities under the Companies Act. As such MAFR reduces the audit committee’s ability to fully discharge its oversight responsibilities and in turn disenfranchises shareholders’ ability to obtain the highest quality audit in the most efficient way.”

(Shango from PWC Inc., p.2, 2017)

From EY Inc.

“Robust independent oversight including inspections and transparency can support audit committees in their statutory role and responsibility towards auditors enabling them to take better, more informed decisions in tender processes and in the (pre)approval of appropriate non-audit services. Robust independent regulatory oversight would contribute to the discharge of audit committees’ responsibilities rather than taking away responsibilities which would be the case with MAFR.”

(Bourne from EY Inc., p.2, 2017)

“Effective (Independent) Engagement Quality Control Review - The engagement quality control review (EQCR) process plays a significant role in ensuring audit quality by providing an independent evaluation of the key judgments made. It serves as a safeguard in ensuring that the audit risks have been appropriately addressed and the audit opinions issued are correct and sufficiently supported. This task is carried out by the engagement quality control reviewer who is experienced and whose role is to challenge the opinion of the key audit partners.”

(Bourne from EY Inc., p.2, 2017)

“Every public and state owned company has to have an audit committee. This is designed to underpin auditor independence.”

(Bourne from EY Inc., p.3, 2017)

“Audit committees should be required to report more detail as regards their interaction with the auditor, including both their consideration of appointments or reappointments and the basis on which they assess the auditor’s effectiveness and their independence. In this connection audit committees should have the option to set a minimum term for the audit engagement mandate. Audit committees could then be required at the end of each mandate to re-assess the audit contract. The shareholders should be informed of the results of the Audit Committee’s reassessment and, when the auditor is proposed for reappointment, their decision to initiate or not a formal tender process.”

(Bourne from EY Inc., p.3, 2017)

“Whilst we understand from the Paper that IRBA have sought the opinion of certain investors on the JSE, we believe that the majority view of shareholders needs to be respected in our democracy. This has been demonstrated in recent Annual General Meetings where voting patterns have indicated the overwhelming majority of shareholders voted in favour of the reappointment of auditors whilst fully informed of the incumbent firm’s length of tenure. We are of the opinion that this is the most appropriate way to approach the matter of auditor appointment with shareholder participation in the decision-making in line with the exercise of their ownership rights.”

(Bourne from EY Inc., p.5, 2017)

“Disenfranchises shareholders and undermines the authority of those charged with corporate governance. By forcing companies to change auditor, audit committees and shareholders are unable to retain the best available firm for the job. The Institute of Directors in South Africa have publicly expressed their views to this effect. This will conflict with directors’ duty to act in the best interest of their company if they believe the incumbent will provide a better quality audit than other available firms. Similarly it will disenfranchise shareholders who are the owners of the company subject to audit. They will not be able to exercise their right to choose the best firm for their audit.”

(Bourne from EY Inc., p.5, 2017)

From Deloitte Inc.

“Clearly, MAFR will directly impact the perceived lack of independence in the case of long firm tenure. However, since the introduction of the IRBA requirement for firms to disclose the length of audit firm tenure at a particular client, audit committees and shareholders (especially the Public Investment Corporation) are well aware of this matter. We have seen this issue receive attention at both audit committee level and at companies’ annual general meetings with a number of listed companies either already changing audit firms or initiating a process to consider a change in audit firm. We believe that this is a sensible approach as those charged with governance, and shareholders, are best placed to balance the risk of long tenure (e.g. perceived or actual lack of independence) with the benefits thereof (e.g. knowledge of the business, understanding of the key risks, etc.).”

(Bam from Deloitte Inc., p.5, 2017)

“The Paper does not consider the existing measures (audit partner rotation, approval of non-audit services, IRBA Code Independence requirements, audit committee verification of auditor independence, etc.) and the effectiveness of these or how these could be enhanced.”

(Bam from Deloitte Inc., p.9, 2017)

“The introduction of MAFR would force the audit committee of a company to change its auditor and would deprive it of its right to make an informed decision in the best interests of the company.”

(Bam from Deloitte Inc., p.11, 2017)

From KPMG Inc.

“MAFR would undermine the audit committee’s ability to choose the best auditor for the job, and determine whether a change in auditor and the timing thereof is in the best interest of the company and its stakeholders.”

(Oddy from KPMG Inc., p.3, 2017)

“Based on the current information in the consultation paper there is no evidence to support that MAFR enhances auditor independence given the extensive governance measures already in place in South Africa.”

(Oddy from KPMG Inc., p.5, 2017)

The South African Institute of Chartered Accountants (SAICA)

“Possible challenges or concerns or disadvantages exceed the potential benefits or advantages, and there should be a greater focus on enhancing measures that already exist rather than adding additional measures, such as MAFR.”

(SAICA, p.5, 2017)

“Participants at the MAFR Indaba called for the IRBA to consider the implications and alignment of requirements dealing with auditor independence in existing legislative frameworks, such as the Companies Act of 2008. This decision has a direct impact on companies and shareholder rights and one would expect that any amendments be made in the Companies Act, considering this Act imposes specific responsibilities on the audit committee as it relates to the appointment of auditors, and affords shareholders specific rights in this regard.”

(SAICA, p.6, 2017)

RESEARCH OBJECTIVE

As the above literature review, existing regulations in South Africa and the summary of certain stakeholder responses to the IRBA consultation paper indicates, there is an important role of professional judgement currently in operation in South Africa. This role of professional judgment, especially that exercised by audit committees and the auditors themselves, appears to be under threat by the prospect of regulation forcing audit firm rotation on South African audit firms. Current regulations allow a high degree of the exercise of judgement on the question of the independence and suitability of the auditor. This judgement is provided by both sides of the audit engagement on JSE listed companies, namely the audit committee exercising its Companies Act statutory duties, and the auditors exercising their responsibilities in terms of professional standards such as the code of ethics governing auditors (the CPC).

The objective of this paper is to document and analyse the opinions of senior audit practitioners regarding whether MAFR regulation of auditor independence removes or reduces the need for stakeholders such as shareholders, audit committees and the auditor themselves to apply professional judgement in regard to auditor independence. It is clear from the official responses of the “big 4” audit firms that audit firm rotation will do that. However, it is important to understand the opinions of individual audit partners and to consider the opinions of non-“big 4” audit firms.

According to Hay (2015) in a paper discussing current auditing areas in need of research, the issues at the frontier of auditing research include two kinds of research questions, namely those that emerge from current practical problems or issues, and those that develop from previous research. According to Hay (2015) a high proportion of research areas in auditing are linked to professional concerns. It is submitted that the role of professional judgment, especially that exercised by audit committees and the auditors, in maintaining auditor independence, is an example of a current practical concern in the MAFR debate and this fact has been established above.

RESEARCH METHODOLOGY

This study is an exploratory study that employs a qualitative research methodology. Qualitative studies aim to explain the ways in which people come to understand and account for issues, events and behaviours in their lives. Therefore the data gathered covers the perceptions, opinions and reasoning of the participants based on their unique experiences of areas related to the topic studied.

Semi-structured interviews were conducted with experienced audit partners across a number of audit firms nationally to understand their individual opinions, not their official audit firm

opinions, with regards to the impact MAFR may have on their exercise of professional judgement.

A semi-structured interview is a qualitative method of inquiry that combines a pre-determined set of open-ended questions (questions that prompt discussion), with the opportunity for the researcher to explore particular themes or responses further. This type of interview does not limit respondents to a set of pre-determined answers, unlike a structured questionnaire for example (Dearnley, 2005). Semi-structured in-depth interviews are the most widely used interviewing format for qualitative research and can occur either with an individual or in groups (DiCicco-Bloom and Crabtree, 2006). The open nature of the questions encourages depth and vitality in the responses by the interviewees and allows new concepts to emerge over the course of the interviews (Dearnley, 2005).

The population and the selection

The population to be analysed are audit practitioners otherwise called “audit partners” or “audit directors”, from the official list of Johannesburg Stock Exchange (JSE) accredited audit firms. Smaller, non-accredited audit firm practitioners have not been considered based on the reasoning that if MAFR is implemented in South Africa it would only apply to JSE listed companies (IRBA, 2016b), which the smaller audit practices do not service with assurance work.

This study employs a purposive sampling technique, also known as judgmental, selective or subjective sampling. Purposive sampling is a type of non-probability sampling which focuses on sampling techniques where the units that are investigated are based on the judgement of the researcher, rather than on statistical techniques (Tongco, 2007). Purposive sampling technique is most effective when one needs to study a certain domain which contains knowledgeable experts. According to Tongco (2007), in choosing a sampling method for informant selection, the question the researcher is interested in answering is of utmost importance and it is especially important to be clear on informant qualifications when using purposive sampling.

Fourteen experienced practicing “registered auditors” were selected from nine different audit firms in order to perform the interview (refer to Table 1 below). According to DiCicco-Bloom and Crabtree (2006) in-depth interviews are used to discover shared understandings of a particular group and the selection of interviewees should be fairly homogenous and share critical similarities related to the research question. This selection of audit partners is therefore the homogenous group that share critical experience related to the research question. The selection is also considered to be fairly representative of the population of registered auditors in South Africa, especially considering that the audit partners selected were involved in the senior leadership of their respective audit practices and were considered sufficiently experienced as audit practitioners, having worked for many years in the capacity of audit partner.

The commonly agreed and recognised distinction between the audit firms (Marx, 2009; Rapoport, 2016) has been used in this study and is as follows:

- “Big four” audit firms refer to the largest four accounting and audit firms globally, namely Deloitte, PricewaterhouseCoopers (PwC), Ernst & Young (EY) and KPMG. These four firms are also referred to as “large-tier” firms (ICAEW, 2016).

- The non-big four firms are either mid-tier or small-tier firms depending on their respective global size, global presence and capabilities as an audit firm in terms of resources (ICAEW, 2016; Rapoport, 2016).

The researchers and the participants in this study used these terms in the interview discussions.

Table 1: Description of the audit partners (participants/respondents) interviewed:

Designation of Participant in Analysis of Results	"Big four" or "Black-owned" firm	"Mid-tier" or "Mid-tier"	Position	Years as Practicing Audit Partner
Audit Partner 1	Big four		Senior Partner	25
Audit Partner 2	Big four		Managing Partner	20
Audit Partner 3	Big four		Senior Partner	25
Audit Partner 4	Big four		Senior Partner	9
Audit Partner 5	Big four		Senior Partner	23
Audit Partner 6	"Black-owned"	Mid-tier	Managing Partner	22
Audit Partner 7	"Black-owned"	Mid-tier	Managing Partner	23
Audit Partner 8	"Black-owned"	Mid-tier	Senior Partner	29
Audit Partner 9	Mid-tier		Managing Partner	32
Audit Partner 10	Mid-tier		Managing Partner	17
Audit Partner 11	Mid-tier		Senior Partner	16
Audit Partner 12	Mid-tier		Managing Partner	33
Audit Partner 13	Mid-tier		Managing Partner	28
Audit Partner 14	Mid-tier		Senior Partner	7

The following is a description of the fourteen practitioners interviewed:

- All the partners were considered senior and highly experienced, ranging between seven and thirty-three years as a practicing audit partner. The average number of years as a practicing registered auditor of all interviewees is 22 years.
- Seven of the partners were either a regional or a national managing partner in the firm and therefore in key leadership and strategic roles within their respective firms. The remainder were senior partners who also held significant leadership responsibilities and portfolios within their respective firms or network of firms.
- The audit firms were selected from Johannesburg and Cape Town offices of the network firms.
- Of the fourteen partners, two were women.
- The two largest black audit firms in South Africa, namely SizweNtsalubaGobodo Inc. and Nkonki Inc. were represented. These two firms are the largest "black-owned" audit firms in South Africa and have grown to considerable size to rival the traditional "mid-tier" firms. Five partners were from the "big four" international audit firms.
- The remaining partners were from the "mid-tier" audit firms (including the "black-owned" medium size firms) who also perform audit services of public interest entities.

Interview process and methodology

Each interview was held in person with the respective participants and lasted between one and two hours, the discussion audio being electronically recorded with the express

permission of each participant. Each participant is held on audio record as giving permission to record the interview, on the condition that all personal names, firm names and client names mentioned in the discussion will not be made publically available or mentioned in any research output produced for public use.

Important Note

The interview questions covered multiple aspects relating to mandatory audit firm rotation (MAFR), however, as outlined in the research objective of this paper, the purpose here is to present and analyse the findings that have a bearing on the aspect of professional judgement. Hence, the open-ended question asked of the participants, relevant to this aspect of MAFR is as follows:

QUESTION: Do you foresee any direct and indirect consequences, including any unintended consequences, of IRBA moving towards MAFR?

The above question is open-ended and did not lead the participant into suggesting that professional judgement (by auditor or audit committee) was under threat. This is important for the methodology of open-ended interviews. The questions should not direct or lead the participants towards preconceived aspects of the study (DiCicco-Bloom and Crabtree, 2006).

According to Leedy and Ormrod (2010), qualitative data analysis ideally occurs concurrently with data collection so that the researcher can generate an emerging understanding about research questions, which in turn informs both the sampling and the questions being asked. This was certainly the case within this study as the interview process was being conducted, as new opinions documented fed into and shaped the subsequent discussions with interviewees. This iterative process of data collection and analysis eventually leads to a point in the data collection where no new categories or themes emerge, referred to as saturation, signaling that data collection is complete (DiCicco-Bloom and Crabtree, 2006). Saturation is believed to have been reached in these interviews in the sense that no new themes or categories surrounding the question of mandatory audit firm rotation (MAFR) emerged in the last interviews, indicating that the selection of fourteen practitioners was sufficient for the purpose of the study, which is to understand the breadth of the concerns and opinions of the audit profession. The selection of participants is not intended to be “representative” of the population, and indeed they cannot be, considering the small percentage of the population represented.

The aim of this research is not to develop new theory, but rather to consider whether mandatory audit firm rotation (MAFR) has the potential to reduce the need for, or practice of, professional judgement to the assessment of auditor independence.

SUMMARY AND DISCUSSION OF THE FINDINGS

All the audit partners agree that the audit engagement and the choice of the auditor, as well as any non-assurance services required, is a decision of both the audit committee, being those charged with governance by the shareholders, as well as the auditors themselves. The audit committee, whose existence is a legislative requirement in South Africa for a public interest entity (section 94 of the Companies Act), is ultimately responsible for the recommendation for the nomination and the replacement of the auditor, subject to approval by the shareholders. The decision of whether or not to ask the auditors for non-assurance

services and whether or not to place the audit out for tender, is ultimately in the hands of the audit committee, being those charged with governance by the shareholders.

All the partners interviewed agreed with the reasoning that the best means of improving auditor independence is actually to improve the quality of corporate governance in the audit clients, rather than through MAFR. Improving the quality of the non-executives on the audit committees, possibly through education and promotion of King III/IV Report principles of corporate governance, was believed to be a means of having a greater impact on auditor independence and audit quality.

Some partners had experience as audit committee members, as well as in their capacity as audit partners, and they expressed that the Audit Committees that they have served on over the years and continue to serve on currently, take auditor independence very seriously. Other partners expressed some mixed experiences regarding the experience and effectiveness of audit committees. South Africa is very highly rated in terms of its standards of corporate governance, namely the World Economic Forum Global Competitiveness Reports (GCR), including the latest 2015-2016 Report (World Economic Forum, 2015). Referring to this fact, many partners stated that, in their experience, often both sides of the audit engagement, the auditor and the audit committee, take independence matters very seriously.

Quote 6 (Audit Partner 1)

“the Audit Committees that I have served on over the years and continue to serve on now take auditor independence very seriously. Our firm and my experience of the other big firms, I can’t talk for the smaller and medium sized firms... the audit firms themselves take auditor independence extremely seriously... If you just consider that South Africa is the pre-eminent market as far as implementation of corporate governance King III etcetera is concerned, it really is at the top of its game. And those Audit Committees are very diligent and they take all of the issues - not just auditor independence, all of their budgetary duties... very seriously.”

Providing examples of strong audit committee action, some partners illustrated that, in their view, when the opposite is the case, i.e. weak governance by the audit committee, this is when there is the greatest potential for independence of the auditor and audit quality to be compromised. Weak audit committees resulted in threats to auditor independence and this should be acknowledged by the IRBA before regulatory changes such as MAFR impose change on the auditors only.

A few audit partners were of the opinion that in their experience there is actually a deficiency in the functioning of the audit committee and this deficiency needs to be addressed before MAFR, or any other audit regulation, is considered. An interesting dissenting view came from a mid-tier firm partner who expressed the occasional failure of audit committees, although the person was in favour of strengthening corporate governance as a better approach than MAFR. In their experience there is a tendency sometimes for audit committees, and audit committee chairpersons, to firstly favour certain audit firms or secondly, not consider the need to replace auditors periodically to remove the familiarity threats.

Quote 10 (Audit Partner 10)

“What we experience is, particularly in the mid-tier, is that, if the FD is a big four, he is totally prejudiced against everybody outside. And normally you will find that, where there is a change, the firm that he trained at, somehow gets included, or ends up getting the job. I am not necessarily talking about listed companies, let’s say larger companies, not listed... And then what we experience with, let’s say larger or mid- sized businesses that are not listed, is that, there’s a perception that they are auditors, it’s almost like it’s a given, it’s almost like he is the manager, it’s like a permanent employment contract in a way... and to remove them is to “fire them”. Yes. So I think [improving governance practices] would improve independence, like as you say the relationship is two-sided and the stricter they are in their corporate governance the better the auditor needs to behave I suppose, if you want to call it that.”

One partner, with extensive experience as both an audit committee member and chairperson, as well as auditor, expressed a concern that in their experience the audit committee’s independence from management can negatively affect their quality as a committee, especially as it related to managing external audit as required by the various codes of corporate governance and the Companies Act. Too often management is handling issues that are clearly the mandate of the audit committee and the audit committee acts as the “rubber stamp”, simply ratifying management’s decision in these issues.

Quote 11 (Audit Partner 7)

“I do believe in the sternness of my profession and I do believe that most of the audit partners and the firms do uphold independence. But there is one thing that is a threat to it. Can I call it a threat? It is the practicality of an audit partner’s wish to retain an audit being linked into the relationship with management. Versus being linked to the audit committee and to the shareholders. For me, that’s the only thing that needs to be changed is if we need to uphold independence.”

Referring to certain key issues that are the responsibility of the audit committee to manage, the above partner made the point that sometimes key issues that should be the jurisdiction of the audit committee were dealt with by management and decided upon, before reaching the audit committee. A number of respondents expressed this concern around management involving themselves in audit committee matters. As it pertains to auditor independence, the problem expressed was that the audit committee receives the result of management decisions regarding key audit issues, such as an audit misstatement uncovered by the auditor, issues around terms of the appointment of the auditor, or non-assurance services to be provided by the auditor. The decision making should however happen the other way around i.e. the audit committee consults with the auditor, makes the relevant decisions, and then notifies management. In this partner’s view, sometimes the audit committee is even guilty of actively requiring the auditor to settle a key issue with management, rather than being the key player in the decision. The specific example given was the audit committee requiring management to approve the audit fee and if they had done so, the committee would simply “rubber stamp” the agreement. Any debate around the audit fee becomes one that is between the auditor and client management, with the audit committee willingly sitting on the side-line, in direct contravention to corporate governance codes of best practice.

Quote 12 (Audit Partner 7)

“Before we even hear about it as the audit committee, management will box it down and these guys are so scared to bring it forward. Then management box it down. By the time it comes to the audit committee it is a “by the way”, watered position. Because the management is there and these guys are presenting and they are really prepared to fight for it. The audit committee normally takes a very bad stance of saying “management sort it out with the auditors”, and for me that is the only thing that threatens the independence of our profession.”

Quote 13 (Audit Partner 7)

“For the audit fee to be approved the audit committee asks ‘have you agreed it [the fee] with management?’ ‘Management do you agree?’ ‘Yes?’, then yes we are happy and it’s done. The moment there is a debate in an audit committee between management and the auditors about the fee the audit committee chair, or the audit committee itself says, ‘please go and sort it out and report back.’”

The respondents often provided examples from past experience, such as one partner describing a situation whereby he/she was a member of an audit committee and management simply told them that the audit was going out for tender. Management then went so far as to provide the audit committee with the short list of firms that had tendered for the role. If this reality presents itself in a company, and if it is tolerated by the audit committee, the result is clearly an ineffective audit committee and poor corporate governance practice. In addition, as this partner points out, if this is the way decisions are made in the company regarding the audit function, the auditors now need to manage their relationship with management. Managing the relationship with management and thereby impairing auditor independence is seen as a necessary means to retain the audit work, since management are effectively performing the role of the audit committee and the non-executives. Therefore this relationship with management creates a clear conflict of interest for the auditor and impairs their independence. It was expressed that if management do not like the auditors or feel that they are too expensive or raising too many audit adjustments, then management can either put the audit out for tender. And this reality is the case regardless of whether there is audit partner or audit firm rotation. The problem exists in both legislated environments, whether there is MAFR or not. Either way there is a lack of independence that will reduce audit quality significantly. It was expressed that this is the problem that the regulator (IRBA) should be looking to address, and MAFR is not the solution. Rather, in the opinion of some of the partners, measures to educate non-executives, and strengthen the corporate governance, will have the greatest impact on auditor independence. Another suggested solution to this was better informed and more active shareholders who ensure the independence of the audit committee board members (non-executives) and who appoint auditors based on this independent recommendation from the audit committee, as is the intention of the Companies Act and the King III/IV Report on governance.

Many respondents expressed similar concerns of a lack of professionalism, knowledge of role and independence in the operations of the audit committee. The partners had experienced many strong and independent audit committees, but unfortunately the “rubber stamp” system is a problem in more than a few companies.

Quote 14 (Audit Partner 6)

"In reality, what I've seen, the audit committee does not use its power at all and in fact you will see and if you track the evolution of the audit profession, there has been concern that management tends to be dominating... they do everything. Virtually all audit opportunities when the client needs a new auditor, management runs the show and in fact it's management's decision and the audit committee frankly, what they do, is rubber stamp."

Some of the audit partners expressed the opinion that the weakness in corporate governance lies not in its principles, as South Africa has some of the best governance principles and structures in the world. All the partners were well aware of the findings of the Global Competitiveness Reports (GCR) in this regard. Rather, the problem lies in its execution in some companies, and of most concern was the need to strengthen the role of the non-executive director. The quality of the non-executive directors needed to be improved in the opinion of many respondents, especially their understanding of King III/IV corporate governance principles, and their degree of independence from the company.

Quote 7 (Audit Partner 12)

"We are 'beating the pack' anyway so why more corporate governance [referring to the Global Competitiveness Reports issued every year by the World Economic Forum]. We are beating the pack worldwide, we have good governance and it's vigorous and you know if you follow the principle set out for the independent non-executives it's that they are not independent. I have a beef with a non-executive director who's been there for twenty years - so where is the rotation? So for twenty years as a non-executive you'd say well you are not independent, so you know rather look at the independence of the non-executive directors through the IOD (Institute of Directors) and other lobby groups and King III as opposed to the auditors. I think the auditors are a lot more independent than the non-executive... so you know you don't want the CEO's friends as non-executives. You want true non-executive directors... but the guys do take their job seriously. Many non-executives take their job seriously. You know our Audit Committees have very vigorous processes. I attend a lot of Audit Committees and it's a very vigorous process. It's dependent on the non-executive and the strength of the non-executives, versus the executives and I think we have got good non-executives [in general] than in some smaller company where it is way too cosy. You know we've had corporate failures where the non-executives have never seen the financials and all those kind of things because those shouldn't be in the profession."

There was a generally expressed concern around the quality and independence of company non-executive directors as specifically identified by other partners. In South Africa, and certainly on exchange listed companies, it is the non-executive directors who comprise the audit committees. Frustration was expressed that the reality of their experience is that non-executive directors are sometimes not being appointed because the shareholders really believe that they should be, or that the audit committee really believes that they are the right firm for the job. The appointment is made because the CEO and CFO believe they should be, and this, in their opinion, is a major problem in South Africa and likely globally. This is a problem that they believe is not being acknowledged and needs to be addressed.

Quote 15 (Audit Partner 7)

“Sometimes I sit back and I say; is it because the audit committee believe they are here because of management? Do they also feel threatened that if management don’t like me, they might say I must actually leave the board? I have often had those couple of questions in my mind - to say it looks like the issue is the lack of independence of the audit committee members in the first place. And now when you start to look into it you start to see the retired [audit] partners, or not necessarily retired partners, but retirees sitting in these audit committees, so it is their only source of income! So maybe it is important for them to keep on, you know. Because now a person is sixty five, seventy... and that’s where they get their income from. So maybe there is reduced independence even at that level.”

Whereas all the audit partners interviewed believed auditor independence can better be established and strengthened through proper corporate governance at the audit client, this should not be construed as though they believe that corporate governance practices in South Africa are weak. On the contrary, a number of audit partners (as above) referred to the GCRs issued every year by the World Economic Forum which rate South Africa’s “strength of auditing and reporting standards” 1st out of 140 countries researched, the “efficacy of corporate boards” 3rd and “strength of investor protection” 14th, based on the 2016 Report (World Economic Forum, 2015). Together with the general recognition that the South African King III Report on Corporate Governance is one on the best governance codes available, it was the opinion of many that the discussion around MAFR should take into account that South Africa is in a strong position from a governance and auditing standards perspective, relative to other developed and developing countries. One partner made the point that, considering the strength of South Africa’s corporate governance and auditing standards, as externally verified, they seriously question the assumption that MAFR would actually improve audit quality. The IRBA needs to answer this question: Will it really improve audit quality? If it cannot be convincingly shown to improve audit quality then it should not be pursued.

Quote 8 (Audit Partner 1)

“the perception might be different [referring to the public’s view of South Africa’s commitment to corporate governance and auditing standards, including its implementation thereof] and so I suppose my point of departure would be I have to seriously question that mandatory rotation is in any way going to [improve audit quality]”

A common concern raised was that MAFR would have the effect of removing the need for much important discussion and decision-making by the audit committees and therefore take away their role as the ultimate “auditor gatekeeper” and assessor of the audit function within the company. Currently the audit committee must, in terms of the Companies Act, approve non-assurance services required of the auditor and formally assess the independence and suitability of the auditor to the company. The feeling was that MAFR would take this important judgement and control away from the audit committee and replace it with simple rotation regulation. The audit committee would no longer have the incentive to take auditor independence and auditor suitability (to the company) seriously. The audit committee would no longer apply its collective mind to the issue of auditor independence, certainly not to the degree expected in terms of corporate governance principles outlined in the King III/IV

Report, because it would be believed that the issue was dealt with by regulation, not by the audit committee. Why should the committee concern itself with threats to auditor independence, especially in light of non-assurance services and familiarity through relationships with management, when the firm would be replaced as a matter of legislation in due course? It was felt (by many partners) that mandatory rotation would artificially limit the freedom of those charged with governance to appoint the audit firm which best meets the needs of the company and its stakeholders.

Quote 9 (Audit Partner 1)

“If I were an Audit Committee member or an Audit Committee Chair, I would resent the responsibility or the power that I inherently have as a non-executive being taken away from me. I would much rather see the focus on improving audit governance. Because that is where the responsibility is. It is the Board of Directors that has the fiduciary duty.” This particular partner is currently, and has been in the past, an audit committee member on public interest entity audit committees.

These views by the partners interviewed reflect a common international argument against MAFR in that auditor rotation would now be arbitrarily forced on a company, regardless of the stage or set of specific circumstances that the company finds itself in. For example, just when a company needs the experience of its long standing auditors, for example in merger or acquisition deals, or in an operational change of direction, which would present significant audit risks, this may coincide with the need to rotate the audit firm, with the incoming audit firm at a significant disadvantage due to unfamiliarity of the client.

All the audit partners interviewed expressed concern over the degree of regulation in the profession. In fact it is fair to say that the issue of over-regulation resulted in the strongest opinions and even frustration amongst the partners. Many were particularly concerned over the public inspections reports performed by the IRBA and feared that additional regulation was damaging the ability of the practitioners to make professional judgement calls, something absolutely necessary in performing an audit, and which the International Standards of Auditing (ISAs) strongly require of the auditor. The concern was simply that MAFR would be another unnecessary regulation in an already over-burdened profession.

Quote 40 (Audit Partner 5)

“So I’m saying there’s a lot there that’s going to lighten or reduce the expectation gap when it comes to stakeholders and users, because they’ll be able to read each audit report [which] will be specific. It’s not going to be a template. They will be able to understand... And independence and all of that, rather than just coming with a rule if it’s mandatory. We are principles-based at the end of the day. And we’re relying on judgement from the profession and from the Audit Committee. Both sides of the engagement are applying their minds and their skills and they’re qualified to do so... Doesn’t that make us a profession? That fact that we exercise professional judgement? We don’t tick boxes. The more we tick boxes... that will directly affect the quality of what we do. That’s where the regulator needs to get a balance... I hope common sense prevails. I think we’ve got a lot of checks and balances in place. I mean enhancing existing structures and I’m not one in favour of rules. We are principle-based, we must deal with it and the King Codes have done tremendous work over the years with the Institute of Directors.”

CONCLUSION

The findings indicate that the audit partner's opinions are mixed regarding their experiences with audit committees. Some believe the standard of audit committee judgement to be of high quality and independent. Some expressed it as sometimes being the opposite, i.e. they have found some audit committees to "cosy up" with management and therefore lose the independent and objective judgement that principles of corporate governance require of them. As such, these audit partners believe that sometimes audit committees are to some degree ineffective and are guilty of "rubber stamping" decisions that management have made already.

However, nearly all the participants acknowledged the world class and internationally recognized corporate governance standards in South Africa, as shown by the annual World Economic Forum Global Competitiveness Reports rankings. This is significant as it stands to reason that if audit committees applied the high quality standards appropriately and if audit committees were appropriately independent of management and experienced, then there would be no auditor independence problems on JSE listed companies. The audit committee is the key gatekeeper of auditor independence and if this role was being performed appropriately then it is submitted that there would be no need for MAFR.

All the partners expressed the opinion that the audit profession, as a profession, is capable of applying its own professional judgement, using the international auditing standard guidelines, to self-assess their independence from the audit client. All the participants believed the existing codes and the five year audit partner rotation rule was sufficient. None of the audit partners were in favour of regulating independence through the use of MAFR.

Professional judgement, as applied by the auditor as a self-assessment of independence, as well as by the audit committee as an independent assessment, was preferred in comparison to legislated audit firm rotation as intended by the regulator. There was a general agreement that audit firm rotation regulation would indeed reduce, or eliminate entirely in some partner's views, the need for professional judgment, and that this would be a mistake.

Limitations of the study

This study is not representative of the audit profession, considering its limited number of participants. In addition, this study analyses only the perceptions and opinions of audit practitioners, albeit very senior practitioners who have extensive experience as engagement partners on public-interest entity audits and in engagements with audit committees and shareholders. Other stakeholder group opinions need to be analysed.

In addition, the research has focused on the use of professional judgement as an alternative to MAFR. No other suitable options were considered but this may be a future area of research.

Finally, a key limitation of the paper is a limitation experienced by much of the international research conducted on MAFR, which is the fact that the study does not consider any measurable effects of MAFR. The most significant academic contributions to the MAFR debate will be the research that analyses the measurable effects of MAFR in jurisdictions whereby MAFR has been implemented. As discussed in the literature review, at least three

such studies have been performed in an Australian, Spanish and Italian context. All three provided findings decidedly against the implementation MAFR, showing that MAFR does not improve auditor independence or financial reporting quality. South African legislators and regulators should consider these findings carefully before making a decision on MAFR. Further research by South African academics is also needed.

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